

2001 Annual Report

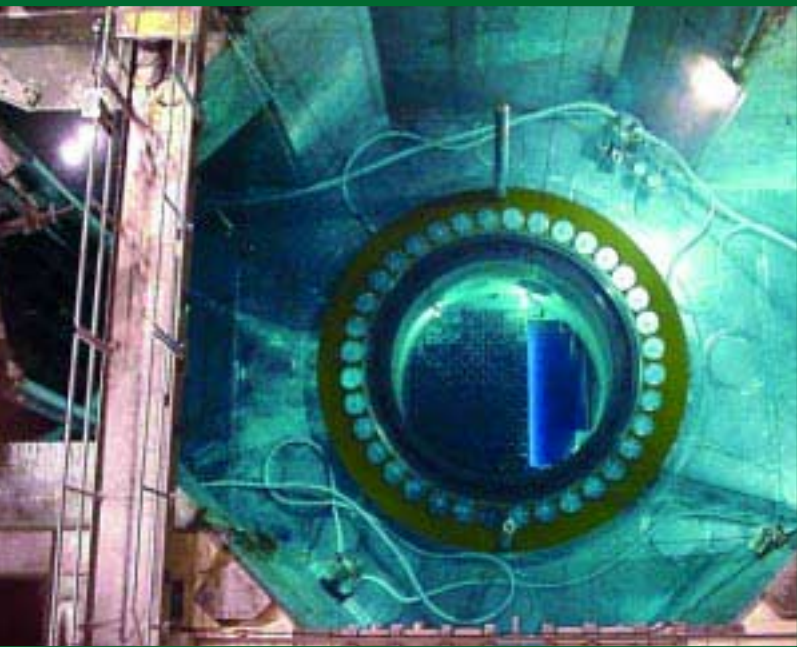
USEC

A Global Energy Company



**FUELING
NUCLEAR
POWER'S
FUTURE**

The Company at the
Core of Global Energy



Fueling Nuclear Power's Future

The Company at the Core of Global Energy

Enriched uranium supplied by USEC is the essential step in preparing nuclear fuel for use in a commercial reactor, so clearly, USEC is fueling nuclear power's future. 2001 will be remembered as the year when nuclear power became part of public policy discussions on how best to meet America's power requirements safely and with a minimum of environmental impact. **Page 4**

2001 ANNUAL REPORT

A World of Potential – USEC sells enriched uranium in 10 countries, including three in Asia where new plants are under construction **7**

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USEC'S ACTIONS AND OUR PERSPECTIVE ON THE FUTURE



James Mellor

A letter from the Chairman James Mellor and President & CEO William Timbers. A strong series of actions brought change to the Company and the nuclear industry in 2001. A report on

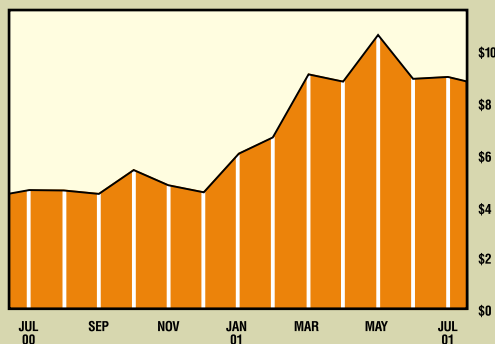
how these initiatives are reinforcing USEC's foundation for a powerful business. **Page 2**



William Timbers

USEC SHARE PRICE

The price of USEC's common stock – which trades as USU on the New York Stock Exchange – improved significantly in fiscal 2001.



USEC Inc. (NYSE:USU) is the world's leading supplier of enriched uranium fuel for commercial nuclear power plants. The Company serves as the United States' executive agent for the national security agreement with Russia to convert nuclear warheads into low-enriched uranium. A global energy company, USEC operates a production facility in Paducah, Kentucky. USEC is headquartered in Bethesda, Maryland, and employs approximately 3,100 people.



Financial Highlights 2001

Fiscal Years Ended June 30	2001	2000	1999
Revenue (in millions)	\$1,143.9	\$1,489.4	\$1,528.6
Net income, excluding special items and inventory valuation adjustment (in millions)	\$ 41.1	\$ 109.1	\$ 120.6
Net income (in millions)	\$ 78.4	\$ 8.9	\$ 152.4
Earnings per share, excluding special items and inventory valuation adjustment	\$.51	\$ 1.20	\$ 1.21
Earnings per share	\$.97	\$.10	\$ 1.52
Net cash provided by operating activities (in millions)	\$ 207.6	\$ 262.8	\$ 230.4
Total debt to capitalization	34%	37%	33%
Annualized dividend per share	\$.55	\$.55	\$ 1.10
Dividend yield as of June 30	6.5%	11.9%	7.4%
Return on average common equity, excluding special items and inventory valuation adjustment	4.2%	11.5%	10.6%



We pushed the envelope of our business in several directions at once during fiscal 2001. We aggressively addressed the challenges before us, while seizing opportunities to build and deliver shareholder value. In the process, we positioned USEC to succeed in a very competitive marketplace. In short, 2001 was a year of accomplishments.

An annual report is by its nature a snapshot in time – a point on a continuum – and while our work is by no means done, we are well on our way to meeting our strategic goals. During the year, our strong actions reinforced the solid business foundation we began several years ago. We are pleased that investors recognized our actions and the improved outlook for nuclear power and rewarded us with a dramatically increased stock price. For the year ended June 30, our stock price rose 82 percent, and with dividends reinvested, the total return for shareholders was 100 percent. This compares quite well with a negative 16 percent return for the S&P 500 index.

Initiative Update

Last year, we laid out a series of initiatives to respond to a bruising business climate for domestic uranium enrichment. We took additional actions in 2001 that will have a powerful, long-term effect on USEC's success. This annual report discusses these actions and initiatives in detail, but here is a brief recap:

- ▶ **We successfully achieved our number one goal of safely consolidating production at a single facility** – on time and on budget. In March 2001, we received approval from the U.S. Nuclear Regulatory Commission to increase the maximum production assay at Paducah. At the same time, we systematically ramped down production at the Portsmouth plant until we ceased enrichment there in May. The Department of Energy has contracted with USEC to maintain the plant until October 2003 in cold standby, a mode that could allow a restart of operations if DOE elected to do so.
- ▶ **We reduced the number of employees at headquarters and both production plants.** As of June 30, 2001, we employ approximately 3,100 people, compared to 3,800 a year ago. Some employees were shifted from production to support DOE's decision to maintain Portsmouth in cold standby, and their positions are funded by the DOE contract. The headquarters staff reductions were part of our action to cut SG&A expenses by 20 percent.



James R. Mellor
Chairman of the Board

► **We took several steps to control our largest cost – electricity.**

USEC secured reliable, competitively priced electricity from the Tennessee Valley Authority for the Paducah plant, monetized \$44 million in excess electricity during the final summer of operating Portsmouth, and negotiated an end to our power contract with the Ohio Valley Electric Corporation that allowed USEC to avoid more than \$400 million in environmental upgrade costs.

► **We reached an agreement in principle to reprice the Russian**

HEU contract. USEC and Tenex, the Russian executive agent for this government-to-government nonproliferation agreement, have agreed on terms to begin market-based pricing in January 2002. Both the United States and Russian governments are reviewing this important new agreement.

► **We actively pursued new enrichment**

technology in order to make our production more cost competitive. In that regard, we continue to evaluate U.S. gas centrifuge and a laser-based process called SILEX, and expect to make a decision in the current fiscal year on the right uranium enrichment technology for USEC.

► **We completed a stock repurchase**

program that bought back more than 20 million shares of the Company's common stock – 20 percent of the shares outstanding – as a tax-efficient means of returning value to shareholders.

► **We requested the U.S. government to initiate proceedings**

against two European competitors that we believe dumped enriched uranium in the U.S. market and received subsidies from their home governments, contrary to U.S. trade laws. In their initial rulings, the Department of Commerce and the International Trade Commission have agreed with our position, and the DOC determined a level of preliminary duties.

Although the decision to pursue this trade case put us at odds with our customers in the short term, we had little choice. Our shareholders were harmed by a serious decline in the price of enriched uranium from dumping and aggressive pricing by competitors intent on wresting away U.S. sales and profits. In the

longer term, we believe our customers will see that we want just what they want: a vibrant marketplace, reasonable prices and a diverse international supply of enriched uranium. A final determination in the case is expected by early next year.

Moving Ahead In 2002

We believe that as a result of the tough decisions we made and the strong actions we took, fiscal 2001 will be remembered as a breakaway year. We made substantial progress, and while we are by no means done, we are heading in the right direction. There are critical issues that must be resolved in the coming months – gaining approval of our market-based pricing agreement for the Russian HEU contract, refining the level of assets and resources needed to operate in a one-plant environment, successfully concluding the trade case and choosing the right future uranium enrichment technology.

This year, many influential people and publications rediscovered the potential of nuclear power. For the first time in years, there is public recognition that nuclear power has an important role to play in America's energy future. We have been spreading that message for many years and we are delighted to be joined by other progressive thinkers. USEC is poised to reap the benefit of a nuclear

renaissance, as the company "Fueling Nuclear Power's Future."

We are pleased to deliver this report to our shareholders on the distinctively positive direction of our Company. Of course, none of these accomplishments would be possible without the hard work and dedication of our employees. Looking ahead, our people are working hard to build shareholder value and bring you another year of accomplishments. ■



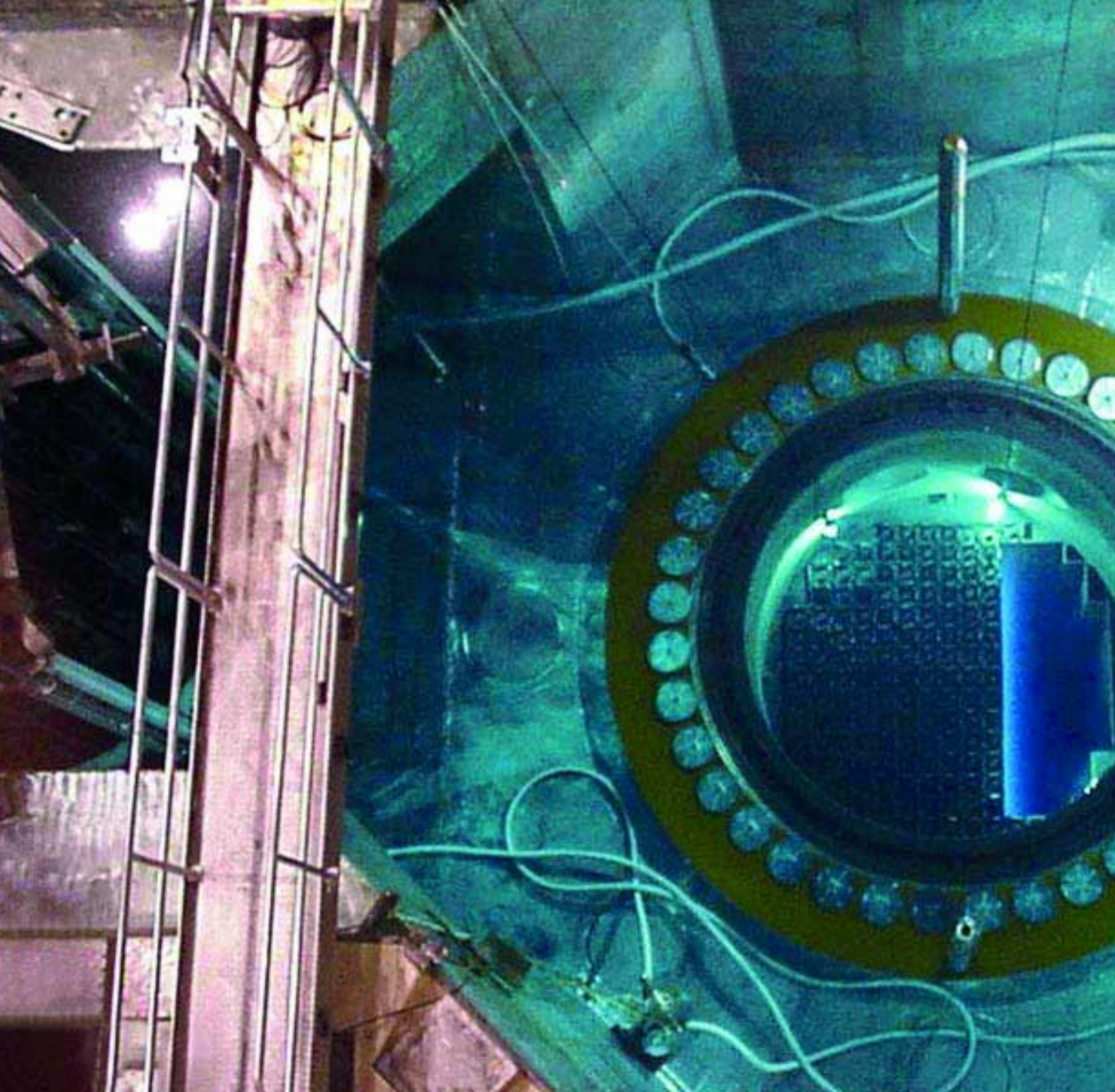
William H. Timbers
President and Chief Executive Officer

Sincerely,

James R. Mellor

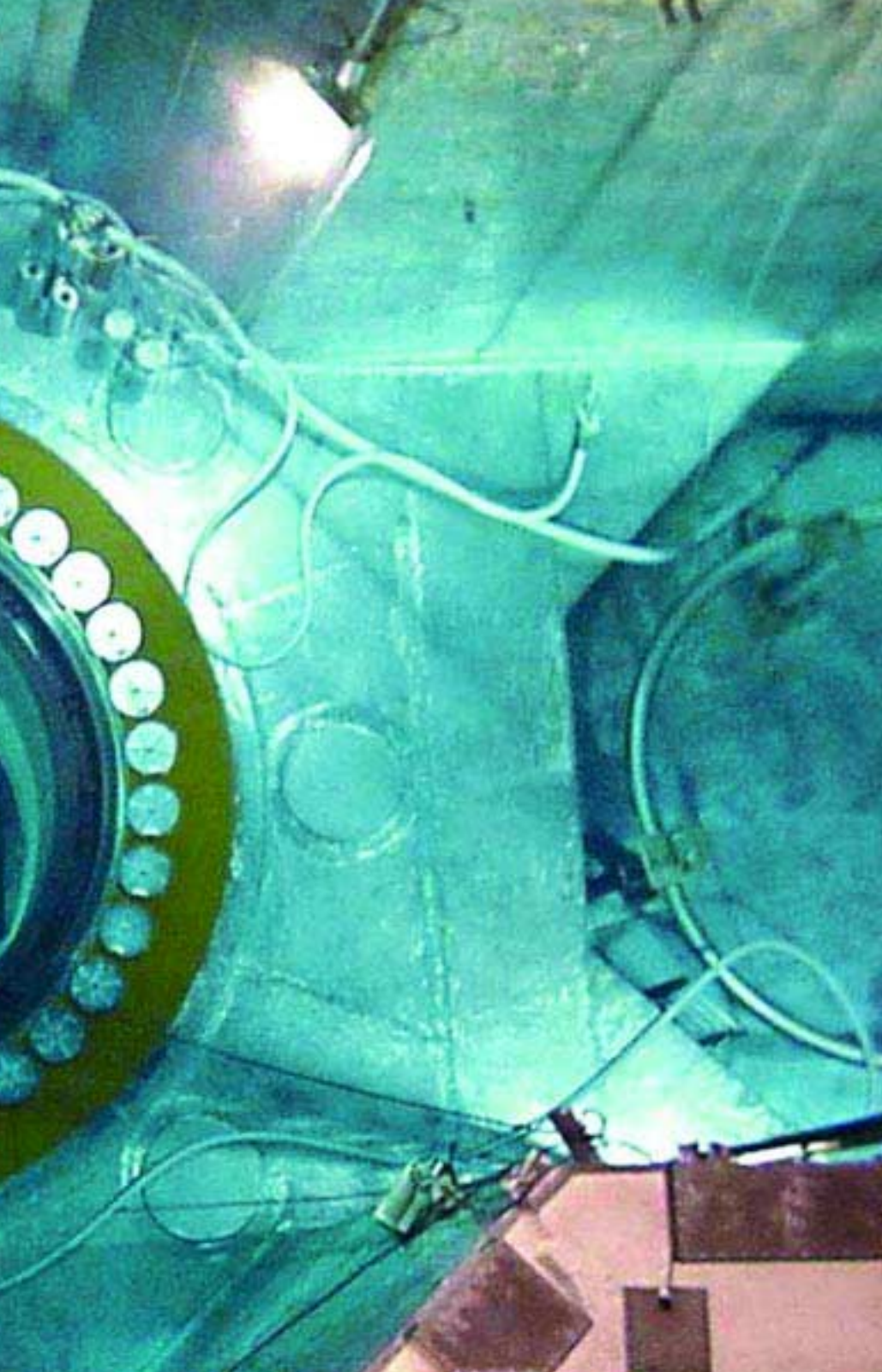
William H. Timbers

September 7, 2001



Looking Directly Into the Core – South Texas Project's reactor is uncovered during refueling and about one-third of the core has been removed. South Texas Project, a USEC customer, had the lowest average fuel cost of any power plant in the United States during 2000.

Fueling Nuclear



2001

will be remembered as the year when it became popular to once again support nuclear power. President George W. Bush and Vice President Dick Cheney voiced their approval. Surveys documented the shift in public opinion. Newspapers across the United States endorsed a fresh look at nuclear power.

USEC has always supported the clean, cost-effective choice for generating electricity for a plugged-in, modern society. Today's headlines show that USEC was ahead of the curve in advocating nuclear energy.

The renaissance of nuclear power is not really a question of if, but rather when. The need for baseload electric generation in the United States is clear – accentuated by shortages in California that have made rolling blackouts across the most populous state an emerging reality. And because it can take several years to build new generating facilities, power shortages could spread to other parts of the country.

Why should nuclear be part of the power generation mix? Because today's efficiently operated nuclear plants are on-line day in, day out for months at a time. According to the Department of Energy, nuclear plants have the lowest fuel cost, helping utilities keep power prices competitive. And nuclear is the environmental choice because there are no emissions to foul our air. Each year, U.S. nuclear power plants prevent 5.1 million tons of sulfur dioxide, 2.4 million tons of nitrogen oxide and 164 million tons of carbon byproducts from entering the earth's atmosphere. As Americans demand more electricity, many experts believe the best way we can maintain clean air is by building new nuclear power plants.

Power's Future

Fueling Nuclear Power's Future

A HANDFUL OF ENRICHED uranium – about a kilogram – has the energy equivalent of about 120 tons of coal, without the emission of greenhouse gases. That's the key to nuclear power's efficiency – uranium fuel that generates clean electricity through a controlled chain reaction.

As it leaves the mine, uranium is approximately one part U²³⁵ and 99 parts U²³⁸. But that is not enough U²³⁵ – the fissionable isotope – to sustain a chain reaction, and so uranium must be enriched in U²³⁵ to be used as fuel. That's where USEC plays a critical role, creating an enriched uranium product that others form into fuel rods that make up the nuclear core of a reactor.

USEC is also the executive agent for a vital non-proliferation

agreement between the U.S. and Russian governments. Under this agreement, USEC takes nuclear material that was formerly the highly enriched uranium core of Soviet-era nuclear weapons and sells the diluted low-enriched uranium to utility customers. This program is better known as "Megatons to Megawatts" (see page 10) and has been responsible for eliminating more than 5,000 nuclear warheads in the past six years.

USEC is proud of its role in peacefully

disposing of these warheads. Most importantly, the Megatons to Megawatts program makes good business sense. As the world leader in the supply of enriched uranium, USEC is uniquely qualified to bring this additional enrichment supply to its customers without disrupting the market. It is smart business to blend U.S. production and Russian warhead material to economically meet the world's requirements for enriched uranium.

USEC is a leader in promoting nuclear as the best choice for meeting America's energy needs. USEC executives have been outspoken advocates of safely expanding nuclear power, speaking before Congress, environmental groups and others. Ours is a symbiotic relationship: the nuclear power industry relies on uranium enrichment, and USEC needs a strong, viable nuclear power industry to thrive and grow. ■



USEC's Product – Cylinders containing low-enriched uranium.

USEC's Key Role In The Nuclear Fuel Cycle

MINING AND MILLING –

Uranium is removed from the earth in the form of ore and then crushed and concentrated.

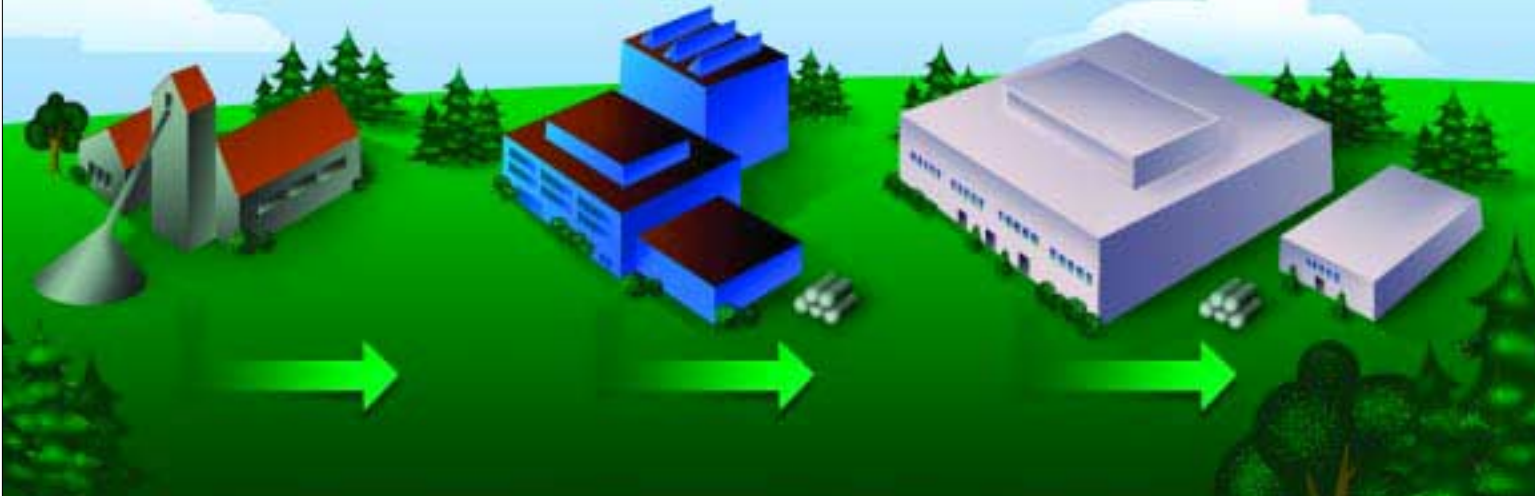
CONVERSION –

Uranium is combined with fluorine gas to produce uranium hexafluoride (UF₆), a powder at room temperature and a gas when heated. UF₆ is next shipped to an enrichment plant.



ENRICHMENT –

Process that increases the concentration of U²³⁵ atoms from its natural state of 0.7% to 3-5%, which is usable as a fuel for commercial nuclear power reactors. USEC has the only enrichment operation in the United States.



USEC SERVES DOZENS OF customers in 10 countries. In fact, in the past year, about half of the Company's revenues came from international sales. USEC representatives work closely with customers to ensure timely shipments of enriched uranium, regardless of its destination. Secure, individual Internet sites allow fuel buyers to check on the status of their orders and account balances at any time, making time zones irrelevant.

USEC is the largest supplier of enriched uranium in Asia where new nuclear plants have been built and more are planned. For example, in Japan, 20 new nuclear power plants are expected to be under construction or completed this decade. USEC has a significant presence in Japan, where long-term contracts are in place with all 10 nuclear utilities. New reactors are also under construction by USEC customers in South Korea and Taiwan. Worldwide, some three dozen reactors are being built. The Energy Information Administration predicts that new generating capacity will need to more than double in the next two decades to meet the power needs of developing countries. ■

USEC's Global Reach



Kashiwazaki-Kariwa Nuclear Power Station – the largest nuclear power station in the world is operated by Tokyo Electric Power Co., USEC's biggest customer. The seven boiling water reactors there generate 8,212 megawatts of electricity.

FUEL FABRICATION – Enriched UF₆ is converted to uranium oxide and formed into small ceramic pellets. These pellets are loaded into metal tubes that form fuel assemblies, which are shipped to nuclear power plants.

NUCLEAR POWER PLANT – Using the energy created from a controlled chain reaction, these facilities generate about 17 percent of the world's electricity.

CONSUMERS – Business and homeowners have come to rely on the steady, baseload electricity supplied by nuclear power and appreciate that there are no emissions of greenhouse gases.



Power Demand Soars

WALK THROUGH MOST NEIGHBORHOODS IN THE United States and chances are you'll see more homes and bigger homes with power-hungry appliances. Computer equipment, multiple televisions, a second refrigerator, and air conditioning all add up to higher demand per household. The 1990's economic expansion also added millions of square feet of air-conditioned office space wired for computers and Internet servers.

The cyber-economy, manufacturing and business cannot function without electricity. Fortunately, America's nuclear power plants are operating at their highest efficiency ever. The Department of Energy reported that in 2000, the 103 U.S. nuclear plants generated a record 754 billion kilowatt-hours of electricity, beating a record set the year before. In 1990, America's then larger fleet of 111 nuclear plants generated just 577 billion kilowatt hours. These higher efficiencies are equivalent to adding 23 one thousand megawatt nuclear plants.

In 2000, the U.S. Nuclear Regulatory Commission (NRC) approved license extensions for six nuclear power plants to operate an additional 20 years. Five additional applications for license extensions for 14 units have been received by the NRC and 24 more are planned for submission by 2004. It now appears that most of America's nuclear reactors will be running for decades to come.

Demand for electricity grew by 2.3 percent annually during the 1990s. Even if demand grows at a more modest 1.8 percent over the next two decades, America may need nearly 400,000 megawatts of new and replacement generating capacity, according to DOE's Energy Information Administration. Industry leaders predict that 50,000 megawatts of that requirement will come from new nuclear power plants over the next 20 years.



American Family – Kitchen appliances, air conditioning and electronic gear are adding to power usage.

What does this mean for USEC? New plants will bring decades of demand for enriched uranium fuel. Better operations and higher capacity factors mean that nuclear plants are using the energy contained in the uranium fuel rods faster, and therefore require more enriched uranium when the plants are refueled. That equates to more sales for USEC.

USEC is customer driven. Its operations are aligned to ensure that it delivers the enriched uranium that customers require. Utilities need a supplier with a record of reliability so that their units are always available during periods of peak demand. The Company has never missed a delivery, and because it maintains a strategic inventory, customers know they can count on USEC to meet their fuel requirements.

USEC is clearly the company at the core of global energy. ■

Speeding Up Refuelings

Ask experts how nuclear plant operators have accomplished the remarkable improvement in performance, and the reason at the top of most lists will be shorter refueling outages.

USEC plays a key role in refueling outages and lowering customers' costs through its Delivery Optimization Program. This program places enriched uranium product at fuel fabricators' facilities at the optimal time to streamline fulfillment of the customers' ultimate requirement: fuel bundles ready to be loaded during a refueling. It also allows



USEC to accommodate last-minute changes to customers' refueling schedules.

Exelon, operator of the largest fleet of nuclear plants in the United States, has demonstrated the best practices for refueling reactors and holds the U.S. record for the shortest refueling outages. In 1997, seven reactors now in Exelon's fleet were refueled in an average of 58 days. Last year, 11 refueling outages lasted an average of 22 days. That performance gives Exelon an extra month of electricity production from its lowest cost generators – and that helps make it more profitable.

Safety Remains Paramount

Safety, efficiency and performance have been three key drivers that have been dominant themes in the Company's business since USEC took over operations in 1993. Recognizing that safe operations are good for business, the Company has taken a proactive approach to promoting a strong safety culture at all of its facilities.

Safety is also the dominant mission of the U.S. Nuclear Regulatory Commission (NRC), the principal agency that oversees our operations. Working closely with the NRC, USEC is diligent in its efforts to earn and maintain the respect and confidence of all its employees, regulators and neighbors in the safety of its operations and the protection of its workers and community. That diligence has been a key

factor in the outstanding safety record achieved by USEC.

USEC has amplified its commitment to safe operations by conducting a safety awareness program in both the Paducah and Portsmouth communities called, "USEC Says, Play It Safe." The Play It Safe campaign appears in local advertisements in newspapers and on radio with home and personal safety tips keyed to seasonal activities.



Safety First, Always – Laretta Hollis, an industrial hygiene technician, inspects and tests air filters prior to issuance. Hollis has worked at Paducah for 25 years without an injury.

Production Consolidated at Paducah

THE NUMBER ONE PRIORITY FOR USEC in fiscal 2001 was the successful consolidation of enrichment operations at Paducah, Kentucky. Although the activities involved in ceasing enrichment at Portsmouth, Ohio, and increasing the enrichment levels at Paducah came to a crescendo in 2001, steps taken years before gave USEC the ability to choose between the two plants.

Structures at Paducah were upgraded for earthquakes over several years, beginning in 1995, to meet tough regulatory standards. The decision to seek approval from the U.S. Nuclear Regulatory Commission for higher assay production was made in 1999. A new competitively priced power contract with the Tennessee Valley Authority was signed in 2000. But the effort to consolidate production at Paducah really went into high gear in fiscal 2001.

Working closely with the NRC, a schedule was developed to meet all regulatory requirements by March. Because electricity costs more and is subject to shortages in the summer months, production is typically ramped down during those months to control costs. Therefore, it was critical that a test run at Paducah be conducted before the summer to prove that the plant could indeed produce commercial-grade enriched uranium.

For nearly 50 years, the Paducah plant performed the first step in the process—increasing U²³⁵ enrichment to about 2 percent before sending product to Portsmouth for further enrichment. Paducah's new mission requires it to enrich uranium to nearly 5 percent U²³⁵, the highest assay required by utility

nuclear reactors. In April, the enriched uranium product coming off the Paducah cascade reached the 5 percent level and stayed there until the plant personnel began bringing production equipment off-line for the summer. The Company's consolidation goal had been successfully achieved.

"Preparing for this upgrade was a complex and challenging task for the plant's managers and employees," said Howard Pulley, Paducah General Manger. "But, we kept safety as our first priority and you could see outstanding teamwork throughout the plant, resolving issues before they became problems.



Nerve center – Paducah control room.

"Our employees, the labor unions and the management team all demonstrated an exceptional commitment to succeed. They repeatedly demonstrated their willingness to go above and beyond expectations to make sure the Paducah plant remains safe, reliable and efficient."

While the Paducah employees had the heady job of upgrading their plant, at Portsmouth the employees had the responsibility of ceasing production and placing

the plant into a standby condition for the Department of Energy (DOE). USEC President William Timbers saluted the Portsmouth plant staff and management for their "strong commitment to safety and the high degree of professionalism they demonstrated in their work as they ended nearly five decades of enrichment operations. They are to be commended for their hard work and their commitment to a safe transition."

The consolidation of production at Paducah allowed the Company to reduce the number of employees involved in enrichment operations. The DOE, which owns the Portsmouth plant, opted to maintain the facility in "cold standby" through September 2003. Approximately 670 USEC employees at Portsmouth will operate the plant in cold standby, remove uranium deposits and winterize the process buildings. USEC employees are conducting this work for the DOE, which is funding the program. Another 585 employees will continue to operate USEC's transfer and shipping facility at Portsmouth.

USEC took a major step toward reducing its potential liabilities during the year when it negotiated a conclusion to obligations under a long-term power contract with the Ohio Valley Electric Co. OVEC had supplied Portsmouth with power since the 1950s under a contract with DOE, but the hundreds of megawatts of electricity were no longer needed at the plant. Under the terms negotiated by USEC, the Company will avoid more than \$400 million in environmental and capital costs at OVEC's coal-burning facilities that would not have benefited USEC. ■



COMMUNITY OUTREACH

The volunteer spirit is alive and well at USEC's Paducah plant as shown by this group of firefighters who put the specialized skills developed on the job to work protecting local residents through service with the West McCracken Fire Department. Shown at the local fire station are firefighters Chuck Bean and Brent Tilford (from left), West McCracken Fire Chief and Paducah Fire Services and Emergency Management Group Manager Don Elrod, and firefighters Larry Adams and David Brown.

USEC has made a strong commitment to the future of its Paducah, Kentucky plant, its employees and the Paducah community. Increasing the plant's enrichment level, making a substantial capital investment in plant upgrades and consolidating its enrichment operations at the Kentucky plant all clearly demonstrate that commitment and USEC's long-term investment in its Paducah plant. The enrichment plant has always enjoyed the strong support of the community.

USEC works hard to partner with both the Paducah and Portsmouth communities in many local efforts and to be a good corporate citizen. Many of USEC's employees at both plants hold leadership roles in local churches, schools, PTAs, government and civic clubs. They coach and mentor young people. They fight fires. They raise money for charities. And they find a thousand other ways to contribute their time and talent to the communities where they live.

Megatons to Megawatts

BOMBS INTO FUEL FOR POWER PLANTS

It is 1992 and the Cold War is over. Bombers and missile batteries are no longer on hair-trigger alert. In fact, many thousands of warheads have been decommissioned. The question before Russian and American leaders: “What can we do with these weapons so that they do not fall into the wrong hands?” The answer: **Megatons to Megawatts.**

This commercial program for nonproliferation and the peaceful recycling of highly enriched uranium (HEU) provides for converting approximately 20,000 Russian nuclear warheads to nuclear plant fuel over a 20-year period. USEC has been the exclusive executive agent for this critical government-to-government foreign policy initiative since the two countries signed the historic agreement in 1993 and the implementing contract in 1994.

By any measure, the program has been highly successful – in large part because of steps taken by USEC to implement the contract and to provide flexibility to its Russian counterpart, Tenex. Together, the partners have reduced the threat to world stability posed by the proliferation of nuclear weapons and materials. The results are impressive:

- ▶ **Since shipments began in 1995, HEU equivalent to 5,000 warheads has been converted to low-enriched uranium (LEU), purchased by USEC and sold to its nuclear utility customers. The commercial use of this material eliminates its potential use as nuclear weapons.**
 - ▶ **USEC has paid Russia approximately \$2 billion to date, providing that country with vital hard currency for a variety of governmental uses, including maintaining nuclear safeguards. Because USEC sells the low-enriched uranium to its customers, the program costs taxpayers nothing.**
 - ▶ **In the early stages of the arrangement, USEC provided substantial financial and technical assistance to Tenex to ensure that the material would meet commercial specifications.**
 - ▶ **USEC and Tenex are 40 percent ahead of the original 20-year schedule to convert a total of 500 metric tons of highly enriched uranium to low-enriched uranium.**
- USEC has taken many additional steps to ensure that Megatons to Megawatts is a success. For example, Russia has unilaterally suspended scheduled deliveries on four occasions for reasons not connected to USEC’s implementation of the contract. USEC has been able to overcome the impact of these delayed shipments by using its own inventory reserves and adjusting its own production schedules to make up the difference.

USEC took these extra steps because it was determined to sustain the program, but more importantly, because the program makes good business sense. USEC has the production capability, inventory and long-term contracts that make it uniquely qualified to bring the Russian nuclear material into the marketplace with the least disruption.

USEC and Tenex reached an agreement in principle in May 2000 on new, market-based commercial pricing terms that would begin in January 2002, when the current contract expires.



Agreement Pending Review

The terms of the proposed amendment to the Megatons to Megawatt contract includes three key elements:

- ▶ A market-based pricing mechanism for purchases of LEU derived from 30 metric tons of Russian warhead HEU each year.
- ▶ Purchase of additional warhead-based LEU through 2004 to make up for previous Russian delivery shortfalls.
- ▶ At Russia's request, the purchase of 3 million commercial SWU from Russia (separate from the HEU program) over a five-year period to supplement revenues to Russia to bridge the transition to market-based pricing.

The Bush Administration has informed the Russian government that it would conduct a review of all U.S. initiatives with Russia. USEC is awaiting completion of this review.

Although pricing under the current agreement does not expire until January 2002, USEC needs to finalize the contract amendment sooner. The ultimate adoption of these new terms will stabilize and ensure successful completion of the HEU agreement over the remaining 13-year period. The Russian HEU represents about 15,000 additional warheads, and the continuation of the agreement meets U.S. national security

and nonproliferation goals at no cost to taxpayers. USEC's purchases provide Russia with the hard currency it needs for its government and for maintaining nuclear safeguards.

The timely adoption of new financial terms – to which both executive agents have

agreed – will preserve the continued success of the program. These new terms enhance the stability and value of the agreement for both parties, should result in a reliable flow of material and further the non-proliferation goals of the United States. ■

Megatons to Megawatts Fast Facts



- ▶ **HEU equivalent to approximately 5,000** former nuclear weapons converted to nuclear fuel since first shipment in 1995.
- ▶ **Calendar year 2000 shipments included** 1038 metric tons of LEU derived from 37 metric tons of HEU. That is equivalent to approximately 1,450 warheads.
- ▶ **HEU is blended down in Russia to less** than 5 percent U²³⁵ assay before shipment to USEC.
- ▶ **Total value of the agreement estimated at** \$12 billion — \$8 billion for the uranium enrichment purchased by USEC and \$4 billion for the natural uranium component, which is sold separately by Russia.
- ▶ **USEC receives no compensation from** the U.S. government for serving as executive agent. All profit is earned from selling the Russian material to utility customers.

Innovation, Flexibility and Dependability Set USEC Apart

AS THE LEADER IN A HIGHLY competitive global environment, USEC has the largest market share for sales of enriched uranium in the U.S. and Asian markets, which are the largest and fastest growing markets, respectively. How did USEC achieve its top position? Through innovation in its contracts, flexibility in its scheduling and dependability of its deliveries.

USEC has built its reputation with customers on these qualities. A good example

of how these qualities are real factors for customers occurred in fiscal 2001. Several Japanese utilities ran into shipping difficulties and needed to identify, then contract with, new shipping agents. In addition, there was a shortage of shipping containers. These adverse developments forced the utilities to rearrange their schedules for shipping enriched uranium and fabricating nuclear fuel. USEC's responsiveness gave them the flexibility they needed to accommodate the scheduling changes, mitigate their shipping problems and meet their refueling requirements. The facts that USEC has never missed a delivery and has inventory flexibility are important factors to our utility customers in evaluating competitive prices and in awarding their business.

On a more routine basis, USEC's Delivery Optimization Program places enriched uranium at fuel fabricators at the most advantageous time to streamline



just-in-time delivery to customers. USEC's sales and marketing team is involved in each step in the process, and customers can check on the progress of their order anytime of the day or night by accessing a secure, individualized Internet site.

Determining just how aggressive the Company should be in going after additional, low-margin sales was an important marketing decision made in 2000. In its last annual report, USEC clearly indicated that it would

not "chase short-term contracts that we consider uneconomical." The Company was also battling the effect of very aggressive pricing and dumping by its European competitors. Following through on that market signal, USEC pulled back from the spot market in fiscal 2001. That action, combined with lower global enrichment capacity from the cessation of operations at Portsmouth and USEC's decision to request the U.S. government to investigate dumping in the United States (see page 13), all contributed to a market price increase of about 20 percent since January 2001 for USEC's product.

Over the long term, USEC's goals are the same as its customers. The Company remains committed to assuring a vibrant marketplace for the nuclear fuel cycle, reasonable prices to ensure that nuclear power stays very competitive and a diverse international supply. ■

OPERATIONS



Dennis Spurgeon

Executive Vice President and COO

In June 2001, Dennis Spurgeon joined USEC as Executive Vice President and Chief Operating Officer. Spurgeon has experience in both the government and commercial enterprise sectors that make him an impressive addition to USEC's senior leadership.

Before joining USEC, Spurgeon was a principal owner and Chief Executive Officer for Swift Group LLC, an international leader in shipbuilding for commercial and military markets. Spurgeon, a graduate of the U.S. Naval Academy and Massachusetts Institute of Technology, has a strong background in nuclear engineering. In addition to working at the U.S. Atomic Energy Commission and at the Energy Research and Development Administration as Assistant Director for Fuel Cycle, Spurgeon has also managed a wide range of nuclear operations in the private sector including General Atomics Company and UNC Resources (formerly United Nuclear Corporation) where he served as Chief Operating Officer.

Spurgeon is responsible for all USEC operations, as well as Marketing and Sales. "This position offers an exciting fulcrum for USEC activities," Spurgeon said. "On one hand, I am working with our production staff to enrich uranium at the lowest cost possible. The other hand is working to ensure our customers' requirements are met as seamlessly as possible while earning our shareholders an attractive return. I am looking forward to the challenges and opportunities ahead."

USEC Takes Action Against Competitors' Dumping

EUROPEAN URANIUM ENRICHERS have dumped low-enriched uranium (LEU) in the United States and received subsidies from their home governments, thereby threatening to materially injure the U.S. enrichment industry. That's the preliminary ruling from the U.S. government in trade investigations initiated at USEC's request against imports produced by two of USEC's competitors.

Faced with declining market prices and the loss of sales due to imports of subsidized European LEU sold at prices below its competitors' production cost plus a reasonable profit, USEC filed a request in December 2000 with the U.S. Department of Commerce (DOC) and the U.S. International Trade Commission (ITC) to investigate these unfair imports.

USEC's goal in requesting the trade investigations was to re-establish fair pricing and competition in the U.S. market. Fair pricing is the foundation for a healthy U.S. nuclear industry and ultimately will protect the competitiveness of nuclear power.

In January 2001, the ITC preliminarily ruled that there is a reasonable indication that these imports threaten to materially injure the domestic enrichment industry.

Subsequently, the DOC requested and obtained thousands of documents detailing the cost of production and sales from the two foreign competitors, Eurodif, S.A., a French government-controlled entity, and the British-Dutch-German consortium, Urenco, Ltd. Based on its findings, the DOC issued preliminary rulings in May and July 2001.

Preliminary Findings

In these preliminary rulings, the DOC estimated duty rates for imported LEU from each of the European producers. In the case of Eurodif, the rate is 3146 percent of the value of imported LEU from France, based on findings of dumping and subsidization. For Urenco, the rate is 707 percent for LEU imports from the United Kingdom, based on findings of dumping and subsidization, and 3.72 percent for imports of LEU from either

the Netherlands or Germany, based on findings of subsidization only.

DOC will make its final determinations in November. If those final rulings determine that either of the competitors' LEU has been dumped or subsidized, the ITC will make a final injury determination in early 2002. An affirmative ruling by the ITC would result in the imposition of duties on imports covered by the ruling.

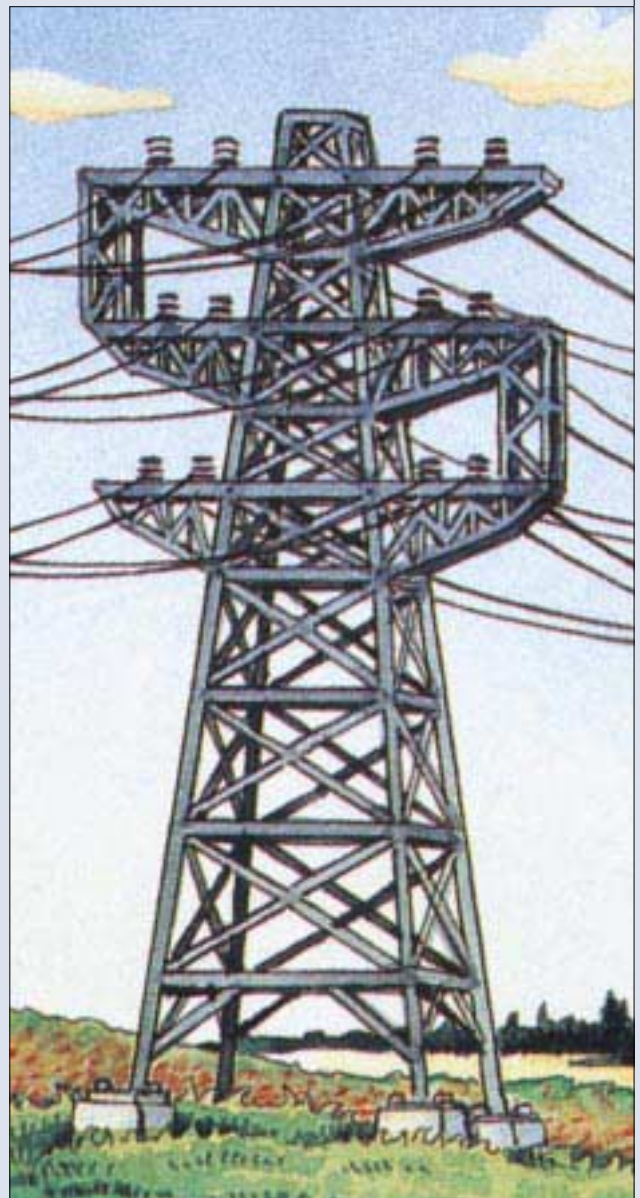
The long- and short-term market prices for the SWU component of the LEU that the Company delivers improved during 2001 in response to several factors, including the investigations. Published price indicators for the long-term market, for example, increased from the mid-\$80s per SWU to \$102 per SWU. Whether these price trends continue will depend on a number of factors, including the results of the trade investigations, the pricing behavior of suppliers in the market, and the market's assumptions about supply and demand for LEU. Because USEC deals mainly in long-term contracts, the higher current prices will have limited impact on its financial results until fiscal 2003 and beyond.

Cost-Competitive Nuclear Fuel

Nuclear fuel constitutes only one-quarter of nuclear power production costs, so the increases in SWU prices so far in 2001 will have little impact on the ultimate price of electricity generated with nuclear power. Significantly,

nuclear fuel costs actually decreased from about 1 cent per kilowatt hour in 1990 to a half cent in 1999. In comparison, the Department of Energy says that the average wellhead price for natural gas more than tripled between 1995 and the middle of 2001, and fuel represents 80 percent of the production cost for electricity generated by natural gas.

Future nuclear power costs are forecast to remain very competitive with coal and stay well below the cost of natural gas and oil. USEC continues its pledge to be fair, reasonable and responsive to its customers regarding the price of its products and to support actions to maintain the competitiveness of nuclear power in the United States and abroad. ■





Selecting the Right Technology

For five decades, huge electric motors at the gaseous diffusion plants have produced enriched uranium through pure brute force. The process pushes uranium hexafluoride (UF₆) gas through a barrier with microscopic holes that separate U²³⁸ from U²³⁵, the fissionable isotope. While this enrichment process has worked well – first for America’s military and later for nuclear power plants – other enrichment companies with newer technology and rising electricity prices have laid out a competitive challenge. The solution? Select an advanced technology that could preserve USEC’s global market leadership position.

The Company evaluated available technological solutions throughout fiscal 2001 and narrowed its focus to two – U.S. advanced gas centrifuge and the SILEX laser-based process. Centrifuge has been deployed for more than two decades and is the technology used by two of USEC’s competitors. The SILEX technology, a third-generation technology to which USEC has exclusive rights, is being developed in Australia.

The centrifuge process uses the physics of spinning motion to separate the uranium elements, just as medical technicians use centrifugal force when separating blood cells. Centrifuge machines spin gaseous UF₆ at very high speeds to separate U²³⁵ from the more abundant U²³⁸ isotope.

The U.S. government conducted research and development on centrifuge technology in the 1970s and 80s, including the construction of centrifuge facilities at the Department of Energy’s Portsmouth,



Advanced Technology – (left, top) USEC has designed a new centrifuge based on DOE’s design, shown above in photograph from mid-1980s. (left, bottom) The SILEX technology is a laser-based process being demonstrated in Australia.

Ohio site. During the past year, USEC and UT-Battelle, the Oak Ridge National Laboratory contractor, worked together under a DOE-approved Cooperative Research and Development Agreement to update earlier designs and to take advantage of advances in composite materials and other technologies. The USEC-led research group has completed 90 percent of centrifuge rotor and end-cap design, which are the most difficult and important components of the centrifuge. USEC is ready to rapidly pursue demonstration of this updated U.S. centrifuge technology.

SILEX, which stands for Separation of Isotopes by Laser Excitation, is an evolutionary improvement in uranium enrichment. USEC has exclusive worldwide rights to this laser-based technology for uranium enrichment. The research is being funded by USEC and conducted in Australia with development partner Silex Systems Ltd.

SILEX uses lasers that are tuned to excite only the U^{235} isotopes and not the U^{238} , enabling separation through a gas dynamic effect. It should have an advantage of using far less electricity than USEC’s current process and should be able to more efficiently separate the two isotopes. In June 2001, the U.S. and Australian governments concluded that SILEX’s potential required that the enrichment technology be classified.

The Company estimates that new enrichment facilities using either the centrifuge or SILEX process could be ready by the end of the decade – ready to meet customers’ needs for enriched uranium to the 2030s and beyond.

Diversification Accelerating

USEC is seeking new opportunities to diversify its revenue base. With the sharp pencil of an accountant, the vision of a strategic thinker and the heart of an entrepreneur, USEC regularly evaluates new revenue sources and profit centers that can add shareholder value.

There are a number of activities that spin off from the Company’s core business of enriching uranium. USEC operates two highly versatile analytical laboratories at Paducah



Diversification – Kimberly Days, a chemist in Spectroscopy and Analytical Support, supports work on Department of Energy assignments for Field Services.

and Portsmouth, providing the DOE and their contractors with a wide range of cost-effective analytical services. In another area of opportunity, USEC submitted a joint venture bid with CH2M Hill, an environmental project development firm, to the DOE to convert depleted UF₆ to a form of uranium that can be safely disposed. The DOE has depleted uranium in thousands of cylinders located at various Portsmouth and Paducah sites. The depleted UF₆ has accumulated since the plants began operations in the 1950s. The DOE is currently evaluating the joint venture’s proposal, which made the DOE’s short list, along with two others. The processing facilities, to be located at both plant sites, are expected to be operational by 2005.

During fiscal 2001, USEC completed processing and disposal of a large amount of used, crushed uranium storage drums and other DOE waste material at the Paducah site. This waste material was commonly referred to as “Drum Mountain.” USEC’s Field Services Group contract with the DOE involved shredding the crushed drums and other materials for disposal at an approved facility. USEC employees are also involved in environmental clean-up work funded by the DOE at both Portsmouth and Paducah.

In a recent development, USEC and two partners submitted a bid to build a 600-

megawatt electricity generating station for the Tennessee Valley Authority near the Paducah plant. Partnering with USEC are Constellation Power Sources of Baltimore, Md. and the Marubeni Corporation of Japan, which could provide project funding.

If selected, the consortium could build the natural gas combined cycle plant on approximately 120 acres just northeast of the Paducah plant. The site may be favorably considered because it can be easily connected to the TVA transmission grid and a natural gas pipeline to supply the power plant is nearby. The partnership’s proposal made TVA’s short list and TVA expects to make a final selection by October.

The cessation of uranium enrichment at Portsmouth opens additional opportunities for diversification. The DOE decided to place the Portsmouth plant until at least October 2003 into “cold standby,” which is a plant condition that would allow the DOE to restart enrichment at a later date. USEC employees are clearly the best qualified for maintaining the plant in that condition, and the DOE has awarded the Company a contract to provide that service. Included under the contract is work to remove deposits within the plant’s cascades and to winterize the plant, which previously stayed heated by the enrichment process. ■



North America



UNITED STATES



MEXICO

USEC has the largest market share for enriched uranium in North America, which includes the United States' 103 operating reactors. Mexico's two nuclear reactors are also USEC customers.

Europe



SPAIN



SLOVENIA



THE CZECH REPUBLIC



BELGIUM



SWITZERLAND

USEC currently serves customers in five European countries. The Company has traditionally held a smaller share of the European market due to the presence of two large competitors.

Asia



JAPAN



SOUTH KOREA



TAIWAN

With a nearly 70 percent market share in Asia, USEC has long-term contracts with customers in Japan, South Korea and Taiwan. New plants are planned or under construction in all three countries.

S E L E C T E D F I N A N C I A L D A T A

Selected financial data should be read in conjunction with the Consolidated Financial Statements and related notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations. Selected financial data as of and for each of the fiscal years in the five-year period ended June 30, 2001, have been derived from the Consolidated Financial Statements which have been audited by Arthur Andersen LLP, independent public accountants.

<i>(millions, except per share data)</i>	2001	2000	Fiscal Years Ended June 30,		
			1999	1998	1997
Statement of Income Data					Predecessor ⁽¹⁾
Revenue:					
Separative work units	\$1,057.3	\$1,387.8	\$1,475.0	\$1,380.4	\$1,551.9
Uranium	86.6	101.6	53.6	40.8	25.9
Total revenue	1,143.9	1,489.4	1,528.6	1,421.2	1,577.8
Cost of sales	991.7	1,236.3	1,182.0	1,062.1	1,162.3
Uranium inventory valuation adjustment	-	19.5	-	-	-
Gross profit	152.2	233.6	346.6	359.1	415.5
Special charges:					
Discontinue uranium enrichment at					
Portsmouth plant	-	126.5 ⁽²⁾	-	-	-
Workforce reductions	-	15.0 ⁽³⁾	-	32.8	-
Suspension of development of AVLIS technology	-	(1.2)	34.7 ⁽⁴⁾	-	-
Privatization costs	-	-	-	13.8	-
Advanced technology development costs	11.4	11.4	106.4	136.7	141.5
Selling, general and administrative	48.8	48.9	40.3	34.7	31.8
Operating income	92.0	33.0	165.2	141.1	242.2
Interest expense	35.2	38.1	32.5	-	-
Other (income) expense, net	(8.1)	(10.5)	(16.8)	(5.2)	(7.9)
Income before income taxes	64.9	5.4	149.5	146.3	250.1
Provision (credit) for income taxes	(13.5)⁽⁵⁾	(3.5)	(2.9) ⁽⁵⁾	-	-
Net income	\$ 78.4	\$ 8.9	\$ 152.4	\$ 146.3	\$ 250.1
Net income per share—basic and diluted	\$.97	\$.10	\$ 1.52		
Dividends per share	\$.55	\$.825	\$.825		
Average number of shares outstanding	80.7	90.7	99.9		

S E L E C T E D F I N A N C I A L D A T A *(continued)*

As of June 30,

<i>(millions)</i>	2001	2000	1999	1998	1997
Balance Sheet Data				Predecessor ⁽¹⁾	
Cash and cash equivalents	\$ 122.5	\$ 73.0	\$ 86.6	\$1,177.8 ⁽⁶⁾	\$1,261.0
Inventories:					
Current assets:					
Separative work units	\$ 918.3	\$ 596.0	\$ 648.8	\$ 687.0	\$ 573.8
Uranium ⁽⁷⁾	178.6	209.8	160.1	184.5	131.5
Materials and supplies	19.0	19.3	22.8	24.8	12.4
Long-term assets	420.2	436.4	574.4	561.0	103.6
Inventories, net	\$1,536.1	\$1,261.5	\$1,406.1	\$1,457.3	\$ 821.3
Total assets	\$2,207.5	\$2,084.4	\$2,360.2	\$3,471.3	\$3,456.6
Short-term debt	—	50.0	50.0	—	—
Long-term debt	500.0	500.0	500.0	—	—
Other liabilities	307.6	281.1	195.0	503.3 ⁽⁸⁾	451.8
Stockholders' equity	972.8	947.3	1,135.4	2,420.5 ⁽⁶⁾	2,091.3
Number of shares outstanding	80.6	82.5	99.2		

1) Selected financial data as of and for each of the fiscal years in the two-year period ended June 30, 1998, have been derived from the financial statements of United States Enrichment Corporation ("Predecessor"), a U.S. Government-owned corporation. In fiscal years 1998 and 1997, there was no short or long term debt, interest expense, provision for income taxes, net income per share, or dividends per share for the Predecessor.

2) The plan to cease uranium enrichment operations at the Portsmouth plant resulted in special charges of \$126.5 million (\$79.3 million or \$.87 per share after tax) in fiscal 2000, including asset impairments of \$62.8 million, severance benefits of \$30.2 million, and lease turnover and other exit costs of \$33.5 million.

3) Workforce reduction plans involving 575 employees resulted in special charges for severance benefits of \$15.0 million (\$9.4 million or \$.10 per share after tax) in fiscal 2000.

4) The suspension of development of the AVLIS enrichment technology resulted in special charges of \$347 million (\$22.7 million or \$.23 per share after tax) in fiscal 1999.

5) The provision for income taxes includes a special income tax credit of \$37.3 million (or \$.46 per share) in fiscal 2001 and \$54.5 million (or \$.54 per share) in fiscal 1999 for deferred income tax benefits that arose from the transition to taxable status. The change in estimate in fiscal 2001 resulted from a reassessment of certain deductions for which related income tax savings were not certain.

6) An exit dividend of \$1,709.4 million was paid to the U.S. Government at the time of the initial public offering in July 1998.

7) Excludes uranium provided by and owed to customers.

8) Other liabilities include accrued liabilities for the disposition of depleted uranium. Pursuant to the USEC Privatization Act, depleted uranium generated by USEC at the time of the initial public offering in July 1998 was transferred to DOE, and, in fiscal 1999, the accrued liability of \$373.8 million for the disposition of depleted uranium was transferred to stockholders' equity.

The following discussion should be read in conjunction with, and is qualified in its entirety by reference to, the Consolidated Financial Statements and related notes appearing elsewhere in this report.

OVERVIEW

USEC, a global energy company, is the world leader in the supply of low-enriched uranium ("LEU") for commercial nuclear power plants. LEU is a critical component in the production of nuclear fuel for nuclear reactors to produce electricity. Based on customers' estimates of their requirements and certain other assumptions, including estimates of inflation rates, at June 30, 2001, USEC had long-term requirements contracts aggregating \$5.4 billion through fiscal 2011 (including \$3.1 billion through fiscal 2004), compared with \$6.1 billion at June 30, 2000.

The standard measure of enrichment in the uranium enrichment industry is a separative work unit ("SWU"). A SWU represents the effort that is required to transform a given amount of natural uranium into two streams of uranium, one enriched in the U²³⁵ isotope and the other depleted in the U²³⁵ isotope, and is measured using a standard formula based on the physics of uranium enrichment. The amount of enrichment contained in LEU under this formula is commonly referred to as the SWU component.

Revenue

Revenue is derived from sales of the SWU component of LEU shipped to customers who supply uranium feedstock to USEC, from sales of the SWU and uranium components of LEU shipped to customers who do not supply feedstock, and from sales of uranium. Since orders for LEU to refuel customer reactors occur once in 12, 18 or 24 months and are large in amount, averaging \$12.0 million per order, the percentage of revenue attributable to any customer or group of customers from a particular geographic region can vary significantly quarter by quarter or year by year. However, customer requirements and orders over the longer term are more predictable.

Agreements with electric utilities are generally long-term requirements contracts under which customers are obligated to purchase a specified percentage of their requirements for the SWU component of LEU. Customers, however, are not obligated to make purchases or payments if they do not have any requirements. There is a trend for contracts with shorter terms that is expected to continue, with the newer contracts generally containing terms in the range of 3 to 7 years.

Revenue and operating results can fluctuate significantly from quarter to quarter, and in some cases, year to year. Customer requirements are determined by refueling schedules for nuclear reactors, which are affected by, among other things, the seasonal nature of electricity demand, reactor maintenance, and reactors beginning or terminating operations. Utilities typically schedule the shutdown of their

reactors for refueling to coincide with the low electricity demand periods of spring and fall. Thus, some reactors are scheduled for annual or biannual refueling in the spring or fall, or for 18-month cycles alternating between both seasons. The timing of larger orders for initial core requirements for new nuclear reactors also can affect operating results.

USEC's financial performance over time can be significantly affected by changes in market prices for SWU. As older contracts expire, USEC's backlog has become more heavily weighted with newer contracts with shorter terms and lower prices. Although USEC expects its backlog will continue to decline over time, the positive impact of higher market prices and new sales commitments will offset in part the impact of shorter term contracts, expiring commitments and lower-priced contracts signed in recent years.

According to industry publications, prices for SWU under new long-term contracts increased 23% to \$102 per SWU since the beginning of fiscal 2001, and uranium prices increased 11% to \$31 per kilogram of uranium hexafluoride over the same period. Since a substantial portion of USEC sales are under long-term contracts, the positive impact of higher market prices today will be recognized in future periods and will help offset lower-priced contracts signed in recent years. Recent market developments that contributed to improvements in market prices for SWU follow:

- ▶ preliminary determinations by the U.S. Department of Commerce ("DOC") that imports by European competitors have been sold at dumped prices and have been subsidized by their foreign governments, and by the International Trade Commission ("ITC") that such imports threaten material injury to the U.S. industry;
- ▶ ceasing uranium enrichment operations at the Portsmouth plant, helping to bring market supply and demand more closely in balance;
- ▶ improved performance of nuclear power plants; and
- ▶ substantial reductions in inventories being sold by secondary suppliers.

Future market prices will depend on the results of the U.S. Government's international trade investigations of LEU imports, fundamental supply and demand shifts, the availability of secondary supplies, and actions of European competitors. An adverse decision in the final phases of the trade investigations could cause a decline in spot and long-term market prices. Increased competition among uranium enrichment suppliers for new sales commitments could cause prices to trend lower.

USEC's contracts are denominated in U.S. dollars, and although revenue has not been directly affected by changes in the foreign exchange rate of the U.S. dollar, USEC may have a competitive price disadvantage or advantage obtaining new contracts in a competitive bidding process depending upon the strength or weakness of the U.S. dollar. Costs of

the primary competitors are denominated in the major European currencies.

Revenue could be negatively impacted by actions of the Nuclear Regulatory Commission ("NRC") suspending operations at domestic reactors. In addition, business decisions by utilities that take into account economic factors, such as the price and availability of alternate fossil fuels, consolidation within the electric power industry, the need for generating capacity and the cost of maintenance, could result in suspended operations or early shutdowns of some reactors.

Cost of Sales

Cost of sales is based on the amount of SWU and uranium sold during the period. Cost of sales for the SWU component of LEU is dependent upon production costs at the plants and purchase costs under the Russian Contract. Production costs consist principally of electric power (representing 52% of production costs in fiscal 2001), labor and benefits, depleted uranium disposition costs, materials, depreciation and amortization, and maintenance and repairs. Under the monthly moving average inventory cost method, an increase or decrease in production or purchase costs will have an effect on costs of sales over future periods.

The plants require substantial amounts of electric power to enrich uranium. In September 2000, USEC began purchasing a substantial portion of the electric power for the Paducah plant at fixed rates pursuant to a power purchase agreement with Tennessee Valley Authority ("TVA"). In fiscal 2001, USEC purchased electric power for the Portsmouth plant from Ohio Valley Electric Corporation ("OVEC"), and purchased a portion of the electric power for the Paducah plant from Electric Energy, Inc. ("EEI"), under long-term power purchase contracts between the U.S. Department of Energy ("DOE") and OVEC and EEI. DOE transferred the benefits of the OVEC and EEI power purchase contracts to USEC. Cost for electric power purchased from OVEC and EEI are based on actual costs incurred by OVEC and EEI and represented 66% of power purchased in fiscal 2001. In fiscal 2002, USEC expects power purchases from TVA will represent 73% of the power supply.

Electric power costs vary seasonally with rates higher during the winter and summer as a function of the extremity of the weather. USEC substantially reduces LEU production and the related power load at the Paducah plant in the summer months when the cost of electric power is high. The electric power load at the Paducah plant is steadily increased after the summer months as production equipment is returned to service.

USEC accrues estimated costs for the future disposition of depleted uranium generated as a result of its operations. Costs are dependent upon the volume of depleted uranium generated and estimated transportation, conversion and disposal costs. USEC stores depleted uranium at the plants and continues to evaluate various proposals for its disposition.

In December 2000, USEC reported to DOE that limited samples of certain natural uranium transferred to USEC from DOE prior to privatization contain elevated levels of technetium that would put the material out of specification. USEC and DOE have agreed on a process, including further sampling, to determine the actual amount of material that may be affected, and that process is underway and expected to be completed in the first half of fiscal 2002, subject to the procedures and time constraints of DOE. The total amount of uranium inventory that may be impacted, if further testing shows that all the material is affected, is approximately 9,500 metric tons with a cost of approximately \$230 million at June 30, 2001. An impairment in the valuation of uranium inventory would result if testing indicates that the material is out of specification and if DOE fails to replace it.

USEC believes, after consultation with legal counsel, that DOE committed itself to transfer non-contaminated material that conforms to regulatory and industry specifications for natural uranium. While no agreement has been reached yet with DOE, USEC expects DOE to replace any material found to be out of specification. Although USEC has sufficient other inventories on hand to meet delivery commitments to customers for the next two years, an impairment in the valuation of uranium inventory would have an adverse impact on USEC's financial condition and results of operations.

USEC is the Executive Agent of the U.S. Government under a government-to-government agreement ("Russian Contract") to purchase the SWU component of LEU recovered from dismantled nuclear weapons from the former Soviet Union for use in commercial electricity production. USEC contracts purchases under the Russian Contract on a calendar year basis. Purchases of the SWU component of LEU from the Russian Federation represented 52% of the combined produced and purchased supply mix for USEC in fiscal 2001, compared with 41% in fiscal 2000. Subject to approval by the U.S. Government of an agreement-in-principle with the Russian Executive Agent, USEC expects SWU purchases from Russia will approximate 60% of the supply mix in fiscal 2002.

USEC reached an agreement-in-principle with the Russian Executive Agent in May 2000 that includes a new market-based pricing agreement under the Russian Contract and an agreement to purchase a fixed quantity of commercial SWU contained in LEU from Russia. The pricing agreement with the Russian Executive Agent is for the period of calendar year 2002 through 2013. Implementation of the agreement is subject to review and approval by the U.S. and Russian Governments and adoption of an amendment to the antidumping suspension agreement between the DOC and the Russian Federation to permit importation of commercial LEU from Russia. The timing and conditions, if any, for approval by the U.S. and Russian Governments are uncertain. If the pricing agreement is not approved, and other pricing

terms are not agreed upon, USEC would have the right to purchase the Russian SWU component of LEU under the Russian Contract for calendar 2002 at calendar 2001 prices. USEC expects the pricing agreement will be finalized before January 2002.

In the event that the new market-based arrangement is not approved by the U.S. and Russian Governments prior to calendar 2002, or if USEC does not have access to anticipated quantities of Russian SWU at anticipated prices, earnings and cash flow in fiscal 2002 would be substantially lower than currently projected, absent USEC making other arrangements.

Under the terms of a 1997 memorandum of agreement between USEC and the U.S. Government, USEC can be terminated, or resign, as the U.S. Executive Agent, or additional executive agents may be named. In either event, any new executive agent could represent a significant new competitor that could adversely affect USEC's profitability and sales.

Update on U.S. Government International Trade Investigations

USEC believes that imports of LEU in the U.S. must conform with trade law requirements of fair pricing in order to maintain long-term domestic enrichment capacity and to promote healthy competition and a strong nuclear fuel cycle. Sustaining a domestic enrichment capability helps ensure U.S. national security and energy security. Accordingly, in December 2000, USEC asked the U.S. Government to initiate an investigation into the pricing of LEU from European suppliers and to restore fair competition in the enrichment market. Specifically, in petitions filed with the DOC and ITC, USEC charged that LEU from Eurodif and its sales agent, Cogema, which are controlled by the French Government, and Urenco, Ltd., a British-Dutch-German consortium, was being sold in the U.S. market below the cost of production plus a reasonable profit and that such production was benefiting from government subsidies in their home markets. USEC further alleged that imports of LEU from these suppliers had materially injured the domestic enrichment industry and threatened to continue to do so in the future.

On December 27, 2000, the DOC initiated the antidumping and countervailing duty investigations requested by USEC, and on January 22, 2001, the ITC ruled that there is a reasonable indication that imports of LEU from the four countries under investigation threaten to cause material injury to the domestic enrichment industry. On May 7, 2001, the DOC preliminarily determined that subsidies were being provided to producers and exporters of LEU from France, Germany, the Netherlands and the United Kingdom, and on July 5, 2001, the DOC preliminarily determined that imports of LEU from France and the United Kingdom were being

sold at less than fair value (i.e., "dumped") in the United States. Pursuant to these findings, the DOC now requires that importers of LEU from France and the United Kingdom post bonds to cover combined antidumping and countervailing duties of 31.46% (if from France) and 7.07% (if from the U.K.) on the value of the LEU, while importers of LEU from Germany and the Netherlands must post bonds to cover countervailing duties of 3.72% on the value of the imported LEU.

Final determinations by the DOC in all investigations are scheduled to be made in November 2001. If the DOC makes final affirmative determinations in any of its investigations, the ITC will then make a final determination regarding material injury or threat of material injury to USEC by reason of these imports. Duties will thereafter be collected on any imports from any country for which the ITC makes an affirmative final determination.

Market prices for SWU in new contracts in the United States have increased since initiation of the investigations. Future expectations of market prices are dependent on the final determinations by the DOC and ITC as well as ongoing competitive pressures. If duties are not imposed on imports of LEU from the countries subject to these investigations, or if the duties are not commercially significant, market prices for SWU and LEU could again be depressed, adversely impacting USEC's future profitability and sales.

Because of the European competitors' aggressive and unfair pricing, USEC has lost a substantial volume of long-term sales in the U.S. market when bidding against Urenco and Eurodif. USEC's backlog of contract commitments has declined and is more heavily weighted with newer contracts with shorter terms and lower prices. In addition, USEC estimates its market share of the SWU component of LEU purchased and shipped to utilities in North America declined to 47% in fiscal 2001, compared with 73% in fiscal 2000, and, in the world market, USEC estimates its market share declined to 29% compared with 35% in fiscal 2000. Movement of customer orders also contributed to the changes in market share in fiscal 2001.

In those instances where USEC has won bids, USEC has had to meet the depressed market price and enter into contracts that are significantly reducing profitability. Because these lost sales and depressed prices generally relate to the SWU component of LEU deliverable under long-term contracts, the adverse impact of these factors on revenue and earnings will be more pronounced in future periods. In addition, if the European competitors' unfair pricing is permitted to continue, USEC will likely lose additional long-term sales in the U.S. market.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS *(continued)*

Results of Operations

The following table sets forth certain items as a percentage of revenue:

	Fiscal Years Ended June 30,		
	2001	2000	1999
Revenue:			
Domestic	49%	62%	62%
Asia	46	32	30
Europe and other	5	6	8
Total revenue	100%	100%	100%
Cost of sales	87	83	77
Uranium inventory valuation adjustment	-	1	-
Gross profit	13	16	23
Special charges	-	10	2
Advanced technology development costs	1	1	7
Selling, general and administrative	4	3	3
Operating income	8	2	11
Interest expense	3	2	2
Other (income) expense, net	(1)	(1)	(1)
Income before income taxes	6	1	10
Provision (credit) for income taxes	(1)	-	-
Net income	7%	1%	10%

RESULTS OF OPERATIONS – FISCAL YEARS ENDED JUNE 30, 2001 AND 2000

Revenue

Revenue from sales of the SWU component of LEU delivered to customers amounted to \$1,057.3 million in fiscal 2001, a reduction of \$330.5 million (or 24%) from \$1,387.8 million in fiscal 2000. The volume sold was 24% lower reflecting movement of customer orders and reductions in commitment levels following aggressive pricing by, and loss of sales to, European competitors. Revenue in fiscal 2001 benefited from a large order from a Japanese customer for initial core requirements of a new reactor, and, in fiscal 2000, revenue benefited from one-time sales to customers in Japan to replace their SWU stranded at the Tokaimura facility in Japan. The average SWU price billed to customers in fiscal 2001 was about the same as in fiscal 2000.

Revenue from sales of uranium, primarily uranium hexafluoride, was \$86.6 million in fiscal 2001, a reduction of \$15.0 million (or 15%) from \$101.6 million in fiscal 2000. The reduction results from lower average sales prices and lower volume sold. USEC continues to focus more on longer-term uranium sales where prices are higher. Prices for natural

uranium improved in fiscal 2001, and revenue from sales of uranium is expected to be higher in fiscal 2002.

Revenue from domestic customers declined \$371.5 million (or 40%), revenue from customers in Asia increased \$49.0 million (or 10%), and revenue from customers in Europe and other areas declined \$23.0 million (or 29%), compared with fiscal 2000. The reduction of 40% in the domestic market reflects substantially lower SWU deliveries from movement of customer orders and reductions in SWU commitment levels following aggressive pricing by European competitors. In the Asian market, revenue in fiscal 2001 benefited from an initial core order for a new reactor and, in fiscal 2000, revenue benefited from replacement SWU sales to Japan.

Cost of Sales

Cost of sales amounted to \$991.7 million in fiscal 2001, a reduction of \$244.6 million (or 20%) from \$1,236.3 million in fiscal 2000. The reductions reflect lower sales of the SWU component of LEU, partly offset by continued higher unit production costs at the plants. Cost of sales continued to be adversely affected by lower production volumes and higher unit costs. USEC increased purchases of the SWU component of LEU imported from Russia and lost sales to aggressive and unfair pricing by foreign competitors. Cost of sales in fiscal 2001 reflects a significant portion of the benefit from the monetization of excess power at the Portsmouth plant in the summer of 2000. As a percentage of revenue, cost of sales amounted to 87%, compared with 83% in fiscal 2000.

Electric power costs amounted to \$331.4 million (representing 52% of production costs) in fiscal 2001, compared with \$329.8 million (representing 50% of production costs) in fiscal 2000. Power costs had been reduced by \$44.0 million in fiscal 2000 from the monetization of excess power at the Portsmouth plant in the summer of 2000. Excluding the monetization of power in fiscal 2000, power costs declined \$42.4 million or 11% in fiscal 2001 reflecting lower production. In September 2000, USEC began purchasing a significant portion of electric power for the Paducah plant at fixed rates from TVA under a 10-year power purchase agreement. In the summer months, USEC substantially reduces production and the related power load at the Paducah plant when the cost of market-based power is high.

Costs for labor and benefits included in production costs declined 7% and the average number of employees at the plants declined 14%, compared with fiscal 2000. Labor costs in fiscal 2001 include costs for a retention bonus program for employees at the Portsmouth plant and a performance bonus program at the plants. Benefit costs include a higher net pension credit in fiscal 2001 from higher expected returns on plan assets and amortization of actuarial gains. The collective bargaining agreement covering 660 hourly employees at the Paducah plant represented by the Paper, Allied-Industrial, Chemical and Energy Workers International Union expired July 31, 2001. The contract renewal process is underway.

Uranium Inventory Valuation Adjustment

Uranium inventories are valued at the lower of cost or market. In fiscal 2000, a uranium inventory valuation adjustment of \$19.5 million was charged against income to reflect spot market prices prevailing at June 30, 2000. Market prices of uranium hexafluoride improved in fiscal 2001 with market prices for uranium hexafluoride at June 30, 2001, quoted 20% higher than June 30, 2000.

Gross Profit

Gross profit amounted to \$152.2 million in fiscal 2001, a reduction of \$81.4 million (or 35%) from \$233.6 million in fiscal 2000. Excluding the uranium inventory valuation adjustment in fiscal 2000, gross profit declined \$100.9 million (or 40%). The lower gross profit reflects the 24% reduction in volume sold and continuing high unit costs from low levels of production at the plants. Gross margin was 13% compared with 16% in fiscal 2000 reflecting higher unit production costs at the plants.

Special Charges

Workforce reduction plans involving 575 employees were finalized in June 2000 and resulted in special charges of \$15.0 million (\$9.4 million or \$.10 per share after tax) for severance benefits in fiscal 2000. Amounts paid and utilized with respect to the workforce reductions involving 483 employees amounted to \$9.7 million in fiscal 2001.

The plan announced in June 2000 to cease uranium enrichment operations at the Portsmouth plant resulted in special charges of \$126.5 million (\$79.3 million or \$.87 per share after tax) in fiscal 2000, including asset impairments of \$62.8 million, severance benefits of \$30.2 million for workforce reductions involving 1,200 plant employees, and lease turnover and other exit costs of \$33.5 million. In May 2001, USEC ceased uranium enrichment operations at the Portsmouth plant and began providing winterization, cold standby and deposit removal services at the Portsmouth plant under contract with DOE. Depending on the timing, implementation and duration of DOE's program for cold standby, costs to cease enrichment operations at the Portsmouth plant accrued by USEC in fiscal 2000 may change. Workforce reductions are delayed as a result of DOE's program to maintain the Portsmouth plant in cold standby. It is not possible to determine the effects of such program on severance and other costs associated with ceasing uranium enrichment operations.

Selling, General and Administrative

Selling, general and administrative expenses amounted to \$48.8 million in fiscal 2001, about the same as in fiscal 2000. Expenses are expected to be 20% lower in fiscal 2002 as a result of workforce reductions, planned reductions in the use of consultants, and the consolidation of office space.

Operating Income

Operating income amounted to \$92.0 million in fiscal 2001 compared with \$33.0 million in fiscal 2000. Special charges had reduced operating income in fiscal 2000.

Interest Expense

Interest expense amounted to \$35.2 million and total interest costs including capitalized interest amounted to \$36.5 million in fiscal 2001, compared with \$38.1 million and \$41.3 million, respectively, in fiscal 2000. The reduction reflects lower average levels of short-term debt outstanding in fiscal 2001.

Provision (Credit) for Income Taxes

The provision (credit) for income taxes in fiscal 2001 includes a special income tax credit of \$37.3 million (or \$.46 per share) resulting from changes in the estimated amount of deferred income tax benefits that arose from the transition to taxable status. USEC transitioned to taxable status in July 1998 at the time of the initial public offering of common stock. The change in estimate resulted from a reassessment of certain deductions for which related income tax savings were not certain.

Excluding the special income tax credit, the effective income tax rate was 37% in fiscal 2001.

Net Income

Excluding the special income tax credit, net income was \$41.1 million (or \$.51 per share) in fiscal 2001, a reduction of \$68.0 million (or 62%) from \$109.1 million (or \$1.20 per share), excluding special charges and the uranium inventory valuation adjustment, in fiscal 2000. The reduction reflects lower gross profit. Net income amounted to \$78.4 million (or \$.97 per share) in fiscal 2001 and \$8.9 million (or \$.10 per share) in fiscal 2000.

The average number of shares of common stock outstanding was 80.7 million in fiscal 2001, a reduction of 10.0 million shares (or 11%) from 90.7 million shares in fiscal 2000. The reduction reflects the repurchase of common stock. At June 30, 2001, there were 80.6 million shares issued and outstanding.

Fiscal 2002 Outlook

USEC reiterates its earnings guidance for fiscal 2002 in a range between \$35 and \$40 million, despite a small loss anticipated in the first quarter of fiscal 2002. Earnings are driven by business performance and will be dependent on the following key factors:

- ▶ implementing an agreement with Russia for market-based pricing under the Russian Contract beginning in January 2002 and obtaining anticipated quantities of Russian SWU;
- ▶ meeting targets for revenue, which is expected to return to fiscal 2000 levels; and
- ▶ meeting targets for lower production costs and lower selling, general, and administrative expenses.

This outlook assumes that cost reductions from the initial year of single plant operations and six months of benefit from purchasing Russian SWU at market-based prices will offset a decline in average SWU selling prices from lower-priced contracts signed in previous years. This outlook also assumes consideration of a change in inventory costing methodology in an effort to improve the matching of inventory costs with sales revenue in a new single operating plant environment. A shift in any of the key factors could have an adverse impact on USEC's earnings and cash flow.

Still pending is completion of the U.S. Government's review of the agreement-in-principle that USEC reached with the Russian Executive Agent last year that includes new market-based pricing under the Russian Contract beginning in January 2002 and the purchase of additional quantities of Russian SWU. USEC's fiscal 2002 earnings and cash flow estimates are based on timely implementation of the new terms. If there is significant delay in the implementation of the new terms, or if USEC is not permitted to purchase anticipated quantities of Russian SWU at anticipated prices, earnings and cash flow in fiscal 2002 will be adversely affected.

USEC ended the year with \$122.5 million in cash and no short-term debt after generating \$154.5 million in cash flow from operations after capital expenditures. USEC continues to forecast cash flow from operations after capital expenditures in fiscal 2002 in the range of negative \$30 to \$50 million as it pays severance benefits and other costs from ceasing uranium enrichment operations at the Portsmouth plant and continues to prudently adjust SWU inventory. USEC has sufficient cash and borrowing capacity to meet anticipated corporate needs, such as dividend payments and capital expenditures. The Company believes that cash flow from operations in years subsequent to fiscal 2002 will return to historical levels.

RESULTS OF OPERATIONS – FISCAL YEARS ENDED JUNE 30, 2000 AND 1999

Revenue

Revenue from sales of the SWU component of LEU amounted to \$1,387.8 million in fiscal 2000, a reduction of \$87.2 million (or 6%) compared with \$1,475.0 million in fiscal 1999. The reduction reflects a decline of 7% in the average SWU price billed to customers.

The volume of SWU sold increased 1% in fiscal 2000 reflecting one-time sales to customers in Japan to replace their SWU stranded at the Tokaimura uranium processing facility in Japan. Operations at the Tokaimura facility were suspended in September 1999 following an incident involving highly enriched uranium for an experimental reactor. LEU supplied by USEC was not involved in the incident. The increase from one-time sales to Japanese customers was offset by lower volume from reductions in commitment levels and the timing of other customer orders.

Revenue from sales of uranium, primarily uranium hexafluoride, amounted to \$101.6 million in fiscal 2000, an increase of \$48.0 million compared with \$53.6 million in fiscal 1999.

Revenue from domestic customers declined \$19.2 million (or 2%), revenue from customers in Asia increased \$25.1 million (or 6%), and revenue from customers in Europe and other areas declined \$45.1 million (or 36%), compared with fiscal 1999. The changes in the geographic mix of revenue resulted from the timing of customer orders, the decline in average SWU prices billed to customers, replacement SWU sales to Japan, and the increase in sales of uranium.

Cost of Sales

Cost of sales amounted to \$1,236.3 million in fiscal 2000, an increase of \$54.3 million (or 5%) compared with \$1,182.0 million in fiscal 1999. Increased purchases of the SWU component of LEU delivered under the Russian Contract and the resulting lower levels of production output and associated higher unit costs at the plants continue to adversely affect cost of sales. Cost of sales in fiscal 2000 reflects the benefit of reductions in power costs from the monetization of excess power at the Portsmouth plant in the summers of 2000 and 1999. As a percentage of revenue, cost of sales amounted to 83%, compared with 77% in fiscal 1999.

Electric power costs amounted to \$329.8 million in fiscal 2000 (representing 50% of production costs) compared with \$436.4 million (representing 57% of production costs) in fiscal 1999, a reduction of \$106.6 million (or 24%). The reduction reflects lower production in fiscal 2000 and an increase in the monetization of excess power at the Portsmouth plant. Under power monetization agreements with DOE and OVEC, USEC released a substantial portion of the electric power for the Portsmouth plant in the summer months. By substantially reducing production and the related power load at the Portsmouth plant USEC monetized its share of the high value power in the summer market. The monetization of excess power resulted in reductions to production costs of \$44.0 million in fiscal 2000 and \$31.7 million in fiscal 1999.

Costs for labor and benefits included in production costs declined 4% compared with fiscal 1999. The average number of employees at the plants declined 7% in fiscal 2000.

Costs for the future disposition of depleted uranium amounted to \$35.3 million in fiscal 2000, a decline of \$5.2 million (or 13%) from \$40.5 million in fiscal 1999. The reduction reflects lower production.

SWU purchased from the Russian Federation represented 41% of the combined produced and purchased supply mix in fiscal 2000, compared with 31% in fiscal 1999.

Uranium Inventory Valuation Adjustment

Spot market prices of uranium were quoted at \$23.62 per kilogram of uranium hexafluoride at June 30, 2000, a decline of 22% compared with June 30, 1999. Since uranium inventories are valued at the lower of cost or market, a non-cash uranium inventory valuation adjustment of \$19.5 million was charged against income in fiscal 2000.

Gross Profit

Gross profit amounted to \$233.6 million in fiscal 2000, a reduction of \$113.0 million (or 33%) compared with \$346.6 million in fiscal 1999. Gross margin was 16% compared with 23% in fiscal 1999. The reduction reflects the 7% decline in average SWU prices billed to customers and the uranium inventory valuation adjustment.

Special Charges

	Balance June 30, 1998	Special Charges	Paid and Utilized	Balance June 30, 1999	Special Charges (Credit)	Paid and Utilized	Balance June 30, 2000
Workforce reductions at the plants	\$12.8	–	\$ (5.9)	\$ 6.9	\$ 15.0	\$ (6.9)	\$15.0
Privatization costs	13.8	–	(13.8)	–	–	–	–
Suspension of development of AVLIS technology	–	\$34.7	(.5)	34.2	(1.2)	(33.0)	–
Discontinue operations at Portsmouth plant:							
Workforce reductions	–	–	–	–	30.2	–	30.2
Lease turnover and other exit costs	–	–	–	–	33.5	(2.8)	30.7
Impairment of property, plant and equipment	–	–	–	–	62.8	(62.8)	–
Total discontinue plant operations	–	–	–	–	126.5	(65.6)	60.9
	\$26.6	\$34.7	\$(20.2)	\$41.1	\$140.3	\$(105.5)	\$75.9

Workforce reduction plans involving 575 employees were finalized in June 2000 and resulted in special charges of \$15.0 million (\$9.4 million or \$.10 per share after tax) for severance benefits in fiscal 2000.

In June 2000, USEC announced that it will cease uranium enrichment operations at the Portsmouth plant as an important step in the ongoing efforts to align production costs with lower market prices. The plan to cease uranium enrichment operations at the Portsmouth plant resulted in special charges of \$126.5 million (\$79.3 million or \$.87 per share after tax) in fiscal 2000, including asset impairments of \$62.8 million, severance benefits of \$30.2 million for workforce reductions involving 1,200 plant employees, and lease turnover and other exit costs of \$33.5 million.

In June 1999, development of the AVLIS enrichment technology was suspended resulting in special charges of \$34.7 million (\$22.7 million or \$.23 per share after tax) for contract terminations, shutdown activities and employee severance and benefit arrangements, of which \$33.5 million had been paid as of June 30, 2000. A cost savings of \$1.2 million was restored to income in fiscal 2000.

Advanced Technology Development Costs

Advanced technology development costs amounted to \$11.4 million in fiscal 2000, a reduction of \$95.0 million compared with \$106.4 million in fiscal 1999. Costs in fiscal 2000 relate to the evaluation of the availability and economics of centrifuge technology and a potential new advanced enrichment technology called SILEX. Costs in fiscal 1999 were primarily

for AVLIS, and development of AVLIS was suspended in June 1999.

Selling, General and Administrative

Selling, general and administrative expenses amounted to \$48.9 million in fiscal 2000, an increase of \$8.6 million (or 21%) compared with \$40.3 million in fiscal 1999. The increase reflects costs for executive compensation plans, including amortization of the cost of restricted stock grants beginning February 1999, and increased consulting fees.

Operating Income

Operating income amounted to \$33.0 million in fiscal 2000, a reduction of \$132.2 million (or 80%), compared with \$165.2 million in fiscal 1999. The reduction resulted primarily from special charges relating to the Portsmouth plant and workforce reductions and lower gross profit in fiscal 2000, partly offset by the reduction in advanced technology development costs following the suspension of AVLIS development in June 1999.

Interest Expense

Interest expense amounted to \$38.1 million in fiscal 2000, an increase of \$5.6 million (or 17%) from \$32.5 million in fiscal 1999. Total interest costs, including capitalized interest, amounted to \$41.3 million compared with \$33.7 million in fiscal 1999. The increase reflects higher average debt levels and higher short-term interest rates in fiscal 2000. Prior to July 28, 1998, the date of the initial public offering,

USEC had no debt. The increase in short-term interest rates reflects changes in market rates and the revisions in USEC's credit ratings in February 2000 to below investment grade.

Other Income

Other income of \$16.8 million in fiscal 1999 included a non-recurring gain of \$8.2 million from a contract modification canceling accrued interest payable on an advance payment from the Arab Republic of Egypt.

Provision for Income Taxes

The provision for income taxes in fiscal 1999 includes a special income tax credit of \$54.5 million (or \$.54 per share) for deferred income tax benefits that arose from the transition to taxable status.

Net Income

Excluding special charges relating to workforce reductions, the plan to cease uranium enrichment operations at the Portsmouth plant and the uranium inventory valuation adjustment, net income was \$109.1 million (or \$1.20 per share) in fiscal 2000. Excluding special charges relating to the suspension of AVLIS and a special tax credit, net income was \$120.6 million (or \$1.21 per share) in fiscal 1999. The reduction of \$11.5 million resulted from lower gross profit, partly offset by lower costs for advanced technology. Net income was \$8.9 million (or \$.10 per share) in fiscal 2000 and \$152.4 million (or \$1.52 per share) in fiscal 1999.

The average number shares of common stock outstanding was 90.7 million, a decline of 9.2 million shares (or 9%) from 99.9 million shares in fiscal 1999. The reduction reflects the repurchase of common stock.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity and Cash Flow

Net cash flow from operating activities amounted to \$207.6 million in fiscal 2001, compared with \$262.8 million in fiscal 2000. Cash flow in fiscal 2001 benefited from a reduction of \$247.3 million in trade receivables from the timing of customer orders and high revenue in the fourth quarter of fiscal 2000 and an increase of \$78.2 million in deferred revenue and advances received from customers, reduced by a substantial buildup of \$322.3 million in SWU inventory as part of the planned consolidation of uranium enrichment operations at the Paducah plant.

Net cash flow from operating activities amounted to \$262.8 million in fiscal 2000, compared with \$230.4 million in fiscal 1999. Cash flow in fiscal 2000 benefited from an inventory reduction of \$122.3 million, primarily from sales of uranium inventories transferred to USEC by DOE at no cash cost prior to the initial public offering. Sales of uranium from inventory provide a direct benefit to cash flow. In addition, cash flow in fiscal 2000 benefited from an increase of \$51.1 million in deferred revenue and advances received from customers and was reduced by payments of \$33.0 million relating to suspension of development of the AVLIS technology.

Capital expenditures of \$53.1 million in fiscal 2001 and \$75.9 million in fiscal 2000 include costs to complete the upgrade of the Paducah plant's capability to produce enriched uranium up to an assay of 5.5%. Capital expenditures in fiscal 2000 included costs for seismic upgrades at the Paducah plant, required by the NRC Compliance Plan, to reduce the risk of release of radioactive and hazardous material in the event of an earthquake. Capital expenditures of \$26.0 million are expected in fiscal 2002.

A total of 20.6 million shares of common stock (or 21% of the shares issued) were repurchased between June 1999 and June 2001 under an authorization by the Board of Directors to repurchase up to 30 million shares by June 2001. There were 2.8 million shares repurchased at a cost of \$13.0 million in fiscal 2001 and 17.0 million shares repurchased at a cost of \$124.6 million in fiscal 2000.

Dividends paid to stockholders amounted to \$44.3 million in fiscal 2001, compared with \$75.9 million in fiscal 2000. In February 2000, the quarterly dividend payment was reduced by half to \$.1375 per share, and there were 11% fewer average shares outstanding in fiscal 2001.

Capital Structure and Financial Resources

In January 1999, USEC issued \$350.0 million of 6.625% senior notes due January 2006 and \$150.0 million of 6.750% senior notes due January 2009. The senior notes are unsecured obligations and rank on a parity with all other unsecured and unsubordinated indebtedness of USEC Inc.

At June 30, 2001, revolving credit commitments of \$150.0 million were available under a bank credit facility scheduled to expire in July 2003. Short-term debt declined by \$50.0 million in fiscal 2001, and there were no short-term borrowings at June 30, 2001. USEC is evaluating several options for replacing the bank credit facility.

At June 30, 2001, USEC was in compliance with financial covenants under the bank credit facility, including restrictions on the granting of liens or pledging of assets, a minimum stockholders' equity and a debt to total capitalization ratio, as well as other customary conditions and covenants. The failure to satisfy any of the covenants would constitute an event of default. The bank credit facility includes other customary events of default, including without limitation, nonpayment, misrepresentation in a material respect, cross-default to other indebtedness, bankruptcy and change of control.

The total debt-to-capitalization ratio was 34% at June 30, 2001, compared with 37% at June 30, 2000.

There are four nuclear reactors operated by two utilities in California. USEC supplies LEU to two reactors under a long-term contract with Pacific Gas and Electric Company ("PG&E"). In April 2001, PG&E declared bankruptcy under Chapter 11 of the federal bankruptcy code. USEC expects to continue to supply LEU to PG&E, and USEC may bid on supplying other reactors not currently under contract. At June 30, 2001, there were no trade receivables outstanding, and there have been no delays in collections or cancelled orders. USEC is closely monitoring the financial problems of the utilities in California and remains committed to protecting its business position and fulfilling its contractual obligations.

USEC expects that its cash, internally generated funds from operating activities, and available financing under the bank credit facility will be sufficient to meet its obligations as they become due, to fund operating requirements of the plants including severance benefits and other shutdown costs at the Portsmouth plant, purchases of the SWU component of LEU delivered to USEC under the Russian Contract, capital expenditures, interest expense, and quarterly dividends.

A summary of working capital at June 30 follows (in millions):

	2001	2000
Cash, net of short-term debt	\$ 122.5	\$ 23.0
Accounts receivable	175.8	423.1
Inventories, net	1,115.9	825.1
Accounts payable and other	(389.9)	(242.8)
Working capital	\$1,024.3	\$1,028.4

ENVIRONMENTAL MATTERS

In addition to costs for the future disposition of depleted uranium, USEC incurs operating costs and capital expenditures for matters relating to compliance with environmental laws and regulations, including the handling, treatment and disposal of hazardous, low-level radioactive and mixed wastes generated as a result of its operations. Operating costs were \$16.5 million, \$18.1 million, and \$24.1 million, and capital expenditures were \$.6 million, \$2.4 million and \$3.1 million in fiscal years 2001, 2000 and 1999, respectively. In fiscal years 2002 and 2003, USEC expects operating costs and capital expenditures for environmental matters to remain at about the same levels as in fiscal 2001.

Environmental liabilities associated with plant operations prior to July 28, 1998, are the responsibility of the U.S. Government, except for liabilities relating to certain identified wastes generated by USEC and stored at the plants. DOE remains responsible for decontamination and decommissioning of the plants.

CHANGING PRICES AND INFLATION

The plants require substantial amounts of electric power to enrich uranium. Information with respect to electric power prices and costs is included above.

A majority of USEC's long-term requirements contracts with customers generally provide for prices that are subject to adjustment for inflation.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

At June 30, 2001, the balance sheet carrying amounts for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and payables under the Russian Contract approximate fair value because of the short-term nature of the instruments.

The fair value of long-term debt is calculated based on a credit-adjusted spread over U.S. Treasury securities with similar maturities. The scheduled maturity dates of long-term debt, the balance sheet carrying amounts and related fair values at June 30, 2001, follow (millions):

	June 30, 2001			
	Maturity Dates		Balance Sheet	
	January 2006	January 2009	Carrying Amount	Fair Value
Long-term debt:				
6.625% senior notes	\$350.0		\$350.0	\$328.4
6.750% senior notes		\$150.0	150.0	131.3
			\$500.0	\$459.7

C O N S O L I D A T E D B A L A N C E S H E E T S

(millions, except share and per share data)

June 30, 2001 June 30, 2000

Assets

Current Assets

Cash and cash equivalents	\$ 122.5	\$ 73.0
Accounts receivable – trade	175.8	423.1
Inventories:		
Separative work units	918.3	596.0
Uranium	178.6	209.8
Uranium provided by customers	21.6	40.2
Materials and supplies	19.0	19.3
Total Inventories	1,137.5	865.3
Other	15.6	23.0

Total Current Assets **1,451.4** 1,384.4

Property, Plant and Equipment, net

189.8 159.3

Other Assets

Deferred income taxes	42.1	10.7
Deferred costs for depleted uranium	27.1	35.4
Prepaid pension assets	76.9	58.2
Inventories	420.2	436.4

Total Other Assets **566.3** 540.7

Total Assets **\$2,207.5** \$2,084.4

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities

Short-term debt	\$ –	\$ 50.0
Accounts payable and accrued liabilities	166.2	164.4
Payables under Russian Contract	100.3	40.5
Deferred revenue and advances from customers	91.0	–
Discontinue uranium enrichment at Portsmouth plant	48.0	60.9
Uranium owed to customers	21.6	40.2

Total Current Liabilities **427.1** 356.0

Long-Term Debt

500.0 500.0

Other Liabilities

Deferred revenue and advances from customers	57.5	70.3
Depleted uranium disposition	66.2	48.6
Postretirement health and life benefit obligations	124.7	106.5
Other liabilities	59.2	55.7

Total Other Liabilities **307.6** 281.1

Commitments and Contingencies (Notes 4, 8 and 9)

Stockholders' Equity

Preferred stock, par value \$1.00 per share, 25,000,000 shares authorized, none issued	–	–
Common stock, par value \$.10 per share, 250,000,000 shares authorized, 100,320,000 shares issued	10.0	10.0
Excess of capital over par value	1,066.9	1,070.7
Retained earnings	39.0	4.9
Treasury stock, 19,754,000 shares and 17,842,000 shares	(142.2)	(135.8)
Deferred compensation	(.9)	(2.5)

Total Stockholders' Equity **972.8** 947.3

Total Liabilities and Stockholders' Equity **\$2,207.5** \$2,084.4

See notes to consolidated financial statements.

C O N S O L I D A T E D S T A T E M E N T S O F I N C O M E

<i>(millions, except per share data)</i>	Fiscal Years Ended June 30,		
	2001	2000	1999
Revenue:			
Separative work units	\$1,057.3	\$1,387.8	\$1,475.0
Uranium	86.6	101.6	53.6
Total revenue	1,143.9	1,489.4	1,528.6
Cost of sales	991.7	1,236.3	1,182.0
Uranium inventory valuation adjustment	-	19.5	-
Gross profit	152.2	233.6	346.6
Special charges:			
Discontinue uranium enrichment at Portsmouth plant	-	126.5	-
Workforce reductions	-	15.0	-
Suspension of development of AVLIS technology	-	(1.2)	34.7
Advanced technology development costs	11.4	11.4	106.4
Selling, general and administrative	48.8	48.9	40.3
Operating income	92.0	33.0	165.2
Interest expense	35.2	38.1	32.5
Other (income) expense, net	(8.1)	(10.5)	(16.8)
Income before income taxes	64.9	5.4	149.5
Provision (credit) for income taxes	(13.5)	(3.5)	(2.9)
Net income	\$ 78.4	\$ 8.9	\$ 152.4
Net income per share – basic and diluted	\$.97	\$.10	\$ 1.52
Dividends per share	\$.55	\$.825	\$.825
Average number of shares outstanding	80.7	90.7	99.9

See notes to consolidated financial statements.

C O N S O L I D A T E D S T A T E M E N T S O F C A S H F L O W S

<i>(millions)</i>	Fiscal Years Ended June 30,		
	2001	2000	1999
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	\$ 78.4	\$ 8.9	\$ 152.4
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	22.6	20.4	16.4
Depleted uranium disposition	25.9	26.1	32.3
Deferred revenue and advances from customers	78.2	51.1	(15.1)
Deferred income taxes	(31.4)	–	–
Special charges:			
Discontinue uranium enrichment at Portsmouth plant	(10.7)	126.5	–
Workforce reductions	(5.2)	15.0	–
Suspension of development of AVLIS technology	–	(33.0)	34.2
Uranium inventory valuation adjustment	–	19.5	–
Changes in operating assets and liabilities:			
Accounts receivable – (increase) decrease	247.3	(49.3)	(137.4)
Inventories – (increase) decrease	(274.0)	122.3	51.2
Payables under Russian Contract – increase	59.8	17.5	78.0
Accounts payable and other liabilities – increase (decrease)	23.5	(62.9)	(1.0)
Other	(6.8)	.7	19.4
Net Cash Provided by Operating Activities	207.6	262.8	230.4
CASH FLOWS USED IN INVESTING ACTIVITIES			
Capital expenditures	(53.1)	(75.9)	(51.1)
CASH FLOWS FROM FINANCING ACTIVITIES			
Repurchase of common stock	(13.0)	(124.6)	(14.8)
Dividends paid to stockholders	(44.3)	(75.9)	(82.5)
Dividends paid to U.S. Treasury	–	–	(1,709.4)
Proceeds from issuance of senior notes	–	–	495.2
Net proceeds from (repayment of) short-term debt	(50.0)	–	50.0
Common stock issued	2.3	–	–
Debt and common stock issuance costs	–	–	(9.0)
Net Cash Provided by (Used in) Financing Activities	(105.0)	(200.5)	(1,270.5)
Net Increase (Decrease)	49.5	(13.6)	(1,091.2)
Cash and Cash Equivalents at Beginning of Fiscal Year	73.0	86.6	1,177.8
Cash and Cash Equivalents at End of Fiscal Year	\$122.5	\$ 73.0	\$ 86.6
Supplemental Cash Flow Information			
Interest paid	\$ 34.4	\$ 40.2	\$ 16.7
Income taxes paid	12.7	3.9	5.7
Supplemental Schedule of Non-Cash Financing Activities			
Transfer of responsibility for depleted uranium disposition to Department of Energy	–	–	373.8

See notes to consolidated financial statements.

C O N S O L I D A T E D S T A T E M E N T S O F S T O C K H O L D E R S ' E Q U I T Y

<i>(millions, except per share data)</i>	Common Stock, Par Value \$.10 per Share	Excess of Capital over Par Value	Retained Earnings	Treasury Stock	Deferred Compensation	Total Stockholders' Equity
Balance at June 30, 1998	\$10.0	\$1,357.1	\$1,053.4	–	–	\$2,420.5
Exit dividend paid to U.S. Treasury	–	(658.0)	(1,051.4)	–	–	(1,709.4)
Transfer of responsibility for depleted uranium to Department of Energy	–	373.8	–	–	–	373.8
Costs related to initial public offering	–	(5.3)	–	–	–	(5.3)
Restricted stock issued, net of amortization	–	4.4	–	–	\$(3.7)	.7
Repurchase of common stock	–	–	–	\$ (14.8)	–	(14.8)
Dividends paid to stockholders	–	–	(82.5)	–	–	(82.5)
Net income	–	–	152.4	–	–	152.4
Balance at June 30, 1999	10.0	1,072.0	71.9	(14.8)	(3.7)	1,135.4
Restricted and other stock issued, net of amortization	–	(1.3)	–	3.6	1.2	3.5
Repurchase of common stock	–	–	–	(124.6)	–	(124.6)
Dividends paid to stockholders	–	–	(75.9)	–	–	(75.9)
Net income	–	–	8.9	–	–	8.9
Balance at June 30, 2000	10.0	1,070.7	4.9	(135.8)	(2.5)	947.3
Restricted and other stock issued, net of amortization	–	(3.8)	–	6.6	1.6	4.4
Repurchase of common stock	–	–	–	(13.0)	–	(13.0)
Dividends paid to stockholders	–	–	(44.3)	–	–	(44.3)
Net income	–	–	78.4	–	–	78.4
Balance at June 30, 2001	\$ 10.0	\$ 1,066.9	\$ 39.0	\$ (142.2)	\$ (.9)	\$ 972.8

See notes to consolidated financial statements.

1. NATURE OF OPERATIONS

USEC Inc., a Delaware corporation (“USEC”), formerly United States Enrichment Corporation (a U.S. Government-owned corporation), is a global energy company and is the world leader in the supply of low-enriched uranium (“LEU”) for use in nuclear power plants. USEC provides LEU to electric utilities for use in about 170 nuclear reactors.

Customers typically deliver uranium feedstock to the enrichment facilities as part of their enrichment contracts. Customers are billed for the separative work units (“SWU”) deemed to be contained in the LEU delivered to them. SWU is a standard unit of measurement which represents the effort required to separate specific quantities of uranium containing .711% of U²³⁵ into two components: enriched uranium having a higher percentage of U²³⁵ and depleted uranium having a lower percentage of U²³⁵. The SWU contained in LEU is calculated using an industry standard formula based on the physics of enrichment.

USEC uses the gaseous diffusion process to enrich uranium, separating and concentrating the lighter uranium isotope U²³⁵ from its slightly heavier counterpart U²³⁸. The process relies on the slight difference in mass between the isotopes for separation. The concentration of the isotope U²³⁵ is increased from less than 1% to up to 5%.

USEC leases the Paducah gaseous diffusion plant located in Paducah, Kentucky, and the Portsmouth gaseous diffusion plant located near Portsmouth, Ohio, from the Department of Energy (“DOE”). In September 2000, USEC began purchasing a substantial portion of the electric power for the Paducah plant at fixed rates pursuant to a power purchase agreement with Tennessee Valley Authority (“TVA”). Power is also purchased by USEC for the Paducah plant under a power contract between the DOE and Electric Energy, Inc. (“EEI”).

In May 2001, USEC ceased uranium enrichment operations at the Portsmouth plant and began providing winterization, cold standby and deposit removal services at the Portsmouth plant under contract with DOE. In fiscal 2001, power for the Portsmouth plant was purchased by USEC under a power contract between DOE and Ohio Valley Electric Corporation (“OVEC”).

The Nuclear Regulatory Commission (“NRC”) has had regulatory authority over the operations of the plants since March 1997. The term of the NRC certification of the plants has been renewed for a five-year period ending December 2003.

USEC has been designated by the U.S. Government as the Executive Agent under a government-to-government agreement and as such entered into an agreement with the Executive Agent for the Russian Federation (the “Russian Contract”) under which USEC purchases the SWU component of LEU derived from highly enriched uranium recovered from dismantled nuclear weapons of the Russian Federation for use in commercial electricity production.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation

USEC Inc. is a holding company. The consolidated financial statements include the accounts of USEC Inc., its principal subsidiary, United States Enrichment Corporation, and its other subsidiaries. All material intercompany transactions are eliminated.

Cash and Cash Equivalents

Cash and cash equivalents include temporary cash investments with maturities of three months or less.

Inventories

Inventories of SWU and uranium are valued at the lower of cost or market. Market is based on the terms of long-term contracts with customers, and, for uranium not under contract, market is based primarily on long-term market prices quoted at the balance sheet date. SWU inventory costs are determined using the monthly moving average cost method and are based on production costs at the plants and purchase costs of the SWU component of LEU under the Russian Contract. Production costs at the plants include electric power, labor and benefits, depleted uranium disposition costs, materials, depreciation and amortization and maintenance and repairs. The cost of the SWU component of LEU purchased under the Russian Contract is recorded at acquisition cost plus related shipping costs.

Property, Plant and Equipment

Construction work in progress is recorded at acquisition or construction cost and includes capitalized interest of \$1.3 million in fiscal 2001 and \$3.2 million in fiscal 2000. Upon being placed into service, costs are transferred to leasehold improvements or machinery and equipment at which time depreciation commences. Leasehold improvements and machinery and equipment are recorded at acquisition cost and depreciated on a straight line basis over the shorter of the useful lives which range from three to ten years or the expected plant lease period which for the Paducah plant is estimated to extend through calendar year 2008. USEC leases most, but not all, of the buildings and facilities at the plants from DOE. At the end of the lease, ownership and responsibility for decontamination and decommissioning of property, plant and equipment that USEC leaves at the plants transfer to DOE. Maintenance and repair costs are charged to production costs as incurred.

In May 2001, USEC ceased uranium enrichment operations at the Portsmouth plant. Special charges in fiscal 2000 include \$62.8 million for the impairment of property, plant and equipment at the Portsmouth plant. USEC continues to operate the transfer and shipping facilities at the Portsmouth plant.

A summary of changes in property, plant and equipment in fiscal years 2001 and 2000 follows (in millions):

	June 30, 1999	Capital Expenditures (Depreciation)	Impairment at Portsmouth Plant	Transfers and Retirements	June 30, 2000	Capital Expenditures (Depreciation)	Transfers and Retirements	June 30, 2001
Construction work in progress	\$ 39.5	\$69.6	\$(12.1)	\$(75.6)	\$ 21.4	\$47.3	\$(44.5)	\$ 24.2
Leasehold improvements	48.5	–	(36.7)	75.5	87.3	4.4	27.1	118.8
Machinery and equipment	157.8	6.3	(53.4)	(2.5)	108.2	1.4	14.8	124.4
	245.8	75.9	(102.2)	(2.6)	216.9	53.1	(2.6)	267.4
Accumulated depreciation and amortization	(79.2)	(20.4)	39.4	2.6	(57.6)	(22.6)	2.6	(77.6)
	\$166.6	\$55.5	\$(62.8)	\$ –	\$159.3	\$30.5	\$ –	\$189.8

Revenue

Revenue from sales of the SWU component of LEU and from sales of uranium is recognized at the time LEU is shipped under the terms of contracts with domestic and foreign electric utility customers. Under power-for-SWU barter contracts, USEC exchanges the SWU component of LEU for electric power supplied to the plants, and revenue is recognized at the time LEU is shipped with selling prices for the SWU component based on the fair market value of electric power received.

Contracts with customers are primarily requirements contracts, under which customers are required to make payment for SWU, uranium or LEU based on their reactor requirements,

whether or not they take delivery. Depending on nuclear reactor refueling requirements, certain customers make advance payments and postpone delivery to a later date. Advances from customers are reported as deferred revenue, and, as LEU is shipped, revenue is recognized. At June 30, 2001, deferred revenue and advances from customers includes a deferred payment obligation of \$40.8 million resulting from the purchase of electric power from TVA in fiscal 2001. The obligation and related interest is scheduled to be satisfied in connection with the sale of SWU to TVA under a requirements contract in fiscal years 2002 through 2004.

No customer represented more than 10% of revenue in fiscal years 2001, 2000, or 1999. Revenue attributed to domestic and international customers follows:

	Fiscal Years Ended June 30,		
	2001	2000	1999
Domestic	49%	62%	62%
Asia	46	32	30
Europe and other	5	6	8
	100%	100%	100%

Financial Instruments

The balance sheet carrying amounts for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, and payables under the Russian Contract approximate fair value because of the short-term nature of the instruments.

Concentrations of Credit Risk

Credit risk could result from the possibility of a customer failing to perform according to the terms of a contract. Extension of credit is based on an evaluation of each customer's financial condition. USEC regularly monitors credit risk exposure and takes steps to mitigate the likelihood of such exposure resulting in a loss. Based on experience and outlook, an allowance for bad debts has not been established for customer trade receivables.

Environmental Costs

Environmental costs relating to operations are charged to production costs as incurred. Estimated future environmental costs, including depleted uranium disposition and waste disposal, resulting from operations where environmental assessments indicate that storage, treatment or disposal is probable and costs can be reasonably estimated, are accrued and charged to production costs.

Advanced Technology Development Costs

Advanced technology development costs are charged to expense as incurred. Costs in fiscal years 2001 and 2000 are for the evaluation of the availability and economics of centrifuge technology and a potential new advanced enrichment technology called SILEX. Costs in fiscal 1999 were primarily for the Atomic Vapor Laser Isotope Separation project ("AVLIS"). Development of the AVLIS technology was suspended in June 1999.

Deferred Income Taxes

USEC follows the asset and liability approach to account for deferred income taxes. Deferred tax assets and liabilities are recognized for the anticipated future tax consequences of temporary differences between the balance sheet carrying amounts of assets and liabilities and their respective tax bases. Deferred income taxes are based on income tax rates in effect for the years in which temporary differences are expected to reverse. The effect on deferred income taxes of a change in income tax rates is recognized in income when the change in rates is enacted in the law.

New Accounting Standards

Under Statement of Financial Accounting Standards No. 143 ("FAS 143"), "Accounting for Asset Retirement Obligations," obligations relating to asset retirements would be recorded on the balance sheet and measured at fair value using an expected present-value technique and a credit-adjusted risk-free interest rate. FAS 143 would become effective and be required to be adopted by USEC at the beginning of fiscal 2003. USEC has not completed its assessment or evaluation of FAS 143 and has not yet determined whether or to what extent the new accounting standards will affect the financial statements.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and reported amounts of revenue and costs and expenses during the periods presented. Estimates include costs for the disposition of depleted uranium, lease turnover activities, ceasing uranium enrichment operations at the Portsmouth plant including decommissioning and postretirement health benefits relating to OVEC power generating facilities and employees, the operating lease periods of the plants, and employee benefits, among others. Actual results could differ from those estimates.

Reclassifications

Certain amounts in the consolidated financial statements have been reclassified to conform with the current presentation.

3. INVENTORIES

Inventories and related balance sheet accounts at June 30 follow (in millions):

	2001	2000
Current assets:		
Separative work units	\$ 918.3	\$ 596.0
Uranium	178.6	209.8
Uranium provided by customers	21.6	40.2
Materials and supplies	19.0	19.3
	1,137.5	865.3
Long-term assets:		
Uranium	230.6	246.4
Highly enriched uranium transferred from DOE	189.6	190.0
	420.2	436.4
Current liabilities:		
Uranium owed to customers	(21.6)	(40.2)
Inventories, net	\$1,536.1	\$1,261.5

In December 2000, USEC reported to DOE that limited samples of certain natural uranium transferred to USEC from DOE prior to privatization contain elevated levels of technetium that would put the material out of specification. USEC and DOE have agreed on a process, including further sampling, to determine the actual amount of material that may be affected, and that process is underway and expected to be completed in the first half of fiscal 2002, subject to the procedures and time constraints of DOE. The total amount of uranium inventory that may be impacted, if further testing shows that all the material is affected, is approximately 9,500 metric tons with a cost of approximately \$230 million at June 30, 2001. An impairment in the valuation of uranium inventory would result if testing indicates that the material is out of specification and if DOE fails to replace it.

USEC believes, after consultation with legal counsel, that DOE committed itself to transfer non-contaminated material that conforms to regulatory and industry specifications for natural uranium. While no agreement has been reached yet with DOE, USEC expects DOE to replace any material found to be out of specification. Although USEC has sufficient other inventories on hand to meet delivery commitments to customers for the next two years, an impairment in the valuation of uranium inventory would have an adverse impact on USEC's financial condition and results of operations.

Inventories of SWU and uranium are valued at the lower of cost or market. Spot market prices of uranium were quoted at \$23.62 per kilogram of uranium hexafluoride at June 30, 2000, a decline of 22% compared with June 30, 1999. Since uranium inventories are valued at the lower of cost or market, a non-cash uranium inventory valuation adjustment of \$19.5 million was charged against income in fiscal 2000. Spot market prices of uranium increased 20% to \$28.25 per kilogram in fiscal 2001.

Inventories included in current assets represent amounts required to meet working capital needs, produce enriched uranium product and balance the uranium and electric power requirements of the plants.

Generally, title to uranium provided by customers remains with the customer until delivery of LEU. USEC holds uranium with estimated fair values of \$817.7 million at June 30, 2001, and \$682.2 million at June 30, 2000, for which title is held by customers and others and for which no assets or liabilities are recorded on the balance sheet. However, uranium provided by customers for which title does pass to USEC prior to delivery of LEU is recorded on the balance sheet at estimated fair values of \$21.6 million at June 30, 2001, and \$40.2 million at June 30, 2000, with corresponding liabilities in the same amounts representing uranium owed to customers.

Inventories reported as long-term assets include uranium not expected to be used or sold within one year of the balance sheet date and include the SWU and uranium components of 50 metric tons of highly enriched uranium transferred to USEC from DOE in fiscal 1998 and scheduled to be blended down to LEU over the next five years. USEC is responsible for costs related to the blending of the highly enriched uranium into LEU, as well as certain transportation, safeguards and security costs.

4. PURCHASE OF SEPARATIVE WORK UNITS UNDER RUSSIAN CONTRACT

In January 1994, USEC on behalf of the U.S. Government signed the 20-year Russian Contract with OAO Technobexport ("Tenex", or "the Russian Executive Agent"), the Executive Agent for the Ministry of Atomic Energy of the Russian Federation, which is the Executive Agent for the Russian Federation, under which USEC purchases the SWU component of LEU derived from up to 500 metric tons of highly enriched uranium recovered from dismantled Soviet nuclear weapons. Highly enriched uranium is blended down in Russia and delivered to USEC, F.O.B. St. Petersburg, Russia, for sale and use in commercial nuclear reactors.

USEC has committed to purchase the SWU component of LEU under the Russian Contract at a cost of \$322.2 million in the six months ending December 31, 2001. The cost of the SWU component of LEU purchased under the Russian Contract, including related shipping charges, in fiscal years 2001, 2000 and 1999 follows (in millions):

	Amount
Fiscal Years Ended June 30,	
2001	\$ 591.5
2000	417.8
1999	319.6
	\$1,328.9

Purchases of the SWU component of LEU from the Russian Federation represented 52% of the combined produced and purchased supply mix for USEC in fiscal 2001, compared with 41% in fiscal 2000. Subject to approval by the U.S. Government of an agreement-in-principle with the Russian Executive Agent, USEC expects SWU purchases from Russia will approximate 60% of the supply mix in fiscal 2002.

USEC reached an agreement-in-principle with the Russian Executive Agent in May 2000 that includes a new market-based pricing agreement under the Russian Contract and an agreement to purchase a fixed quantity of commercial SWU contained in LEU from Russia. The pricing agreement with the Russian Executive Agent is for the period of calendar year 2002 through 2013. Implementation of the agreement is subject to review and approval by the U.S. and Russian Governments and adoption of an amendment to the anti-dumping suspension agreement between the DOC and the Russian Federation to permit importation of commercial LEU from Russia. The timing and conditions, if any, for approval by the U.S. and Russian Governments are uncertain. If the pricing agreement is not approved, and other pricing terms are not agreed upon, USEC would have the right to purchase the Russian SWU component of LEU under the Russian Contract for calendar 2002 at calendar 2001 prices. USEC expects the pricing agreement will be finalized before January 2002.

5. INCOME TAXES

The provision (credit) for income taxes follows (in millions):

	Fiscal Years Ended June 30,		
	2001	2000	1999
Current:			
Federal	\$ 16.4	\$(2.1)	\$ 5.1
State and local	1.5	.8	.6
	17.9	(1.3)	5.7
Deferred:			
Federal	5.4	(2.1)	40.7
State and local	.5	(.1)	5.2
	5.9	(2.2)	45.9
Special deferred tax credit from transition to taxable status:			
Federal	(34.3)	–	(49.8)
State and local	(3.0)	–	(4.7)
	(37.3)	–	(54.5)
	\$(13.5)	\$(3.5)	\$ (2.9)

The provision (credit) for income taxes includes a special income tax credit of \$37.3 million in fiscal 2001 and \$54.5 million in fiscal 1999 for deferred income tax benefits that arose from the transition to taxable status. USEC transitioned to taxable status in July 1998 at the time of the initial public offering. The change in estimate in fiscal 2001 resulted from a reassessment of certain deductions for which related income tax savings were not certain.

Future tax consequences of temporary differences between the carrying amounts for financial reporting purposes and USEC's estimate of the tax bases of its assets and liabilities result in deferred tax assets and liabilities at June 30, as follow (in millions):

	2001	2000
Deferred tax assets:		
Plant lease turnover and other exit costs	\$34.2	\$30.9
Employee benefits costs	16.3	15.2
Property, plant and equipment	–	5.4
Tax intangibles	13.1	54.8
Deferred costs for depleted uranium	26.7	–
Tax credit carryforward	–	4.2
Other	5.8	12.9
	96.1	123.4
Valuation allowance	(45.2)	(82.5)
Deferred tax assets, net of valuation allowance	50.9	40.9
Deferred tax liabilities:		
Depleted uranium disposition	–	13.5
Inventory costs	8.8	16.7
Deferred tax liabilities	8.8	30.2
	\$42.1	\$10.7

USEC became subject to federal, state and local income taxes at the time of the initial public offering in July 1998. The valuation allowance of \$45.2 million at June 30, 2001, and \$82.5 million at June 30, 2000, relates to various deferred tax items and valuations resulting from the privatization.

Excluding the special tax credit of \$37.3 million in fiscal 2001, the provision for income taxes amounted to \$23.8 million and is based on effective tax rate of 37%. A reconciliation of income taxes calculated based on the statutory federal income tax rate of 35% and the provision (credit) for income taxes reflected in the consolidated statements of income follows (in millions):

	Fiscal Years Ended June 30,		
	2001	2000	1999
Federal income taxes based			
on statutory rate	\$ 22.7	\$ 1.9	\$ 52.3
State income taxes, net of			
federal benefit	3.4	.2	3.4
Export tax incentives	(3.6)	(3.9)	(1.4)
Research and experimentation			
tax credit	–	(1.7)	(3.4)
Other	1.3	–	.7
	23.8	(3.5)	51.6
Special deferred tax credit from			
transition to taxable status	(37.3)	–	(54.5)
	\$(13.5)	\$(3.5)	\$(2.9)

6. SHORT AND LONG-TERM DEBT

Short and long-term debt at June 30 follows (in millions):

	2001	2000
Short-term debt	\$ –	\$ 50.0
Long-term debt:		
6.625% senior notes, due		
January 20, 2006	350.0	350.0
6.750% senior notes, due		
January 20, 2009	150.0	150.0
	\$500.0	\$550.0

In January 1999, USEC issued \$350.0 million of 6.625% senior notes due January 20, 2006, and \$150.0 million of 6.750% senior notes due January 20, 2009, resulting in net proceeds of \$495.2 million. The senior notes are unsecured obligations and rank on a parity with all other unsecured and unsubordinated indebtedness of USEC Inc. The senior notes are not subject to any sinking fund requirements. Interest is paid every six months on January 20 and July 20. The senior notes may be redeemed at any time at a redemption price equal to the principal amount plus any accrued interest up to the redemption date plus a make-whole premium, as defined.

At June 30, 2001, revolving credit commitments of \$150.0 million were available under a bank credit facility scheduled to expire in July 2003. There were no short-term borrowings at June 30, 2001. At June 30, 2000, short-term debt amounted to \$50.0 million with weighted average interest rate of 7.7%.

At June 30, 2001, USEC was in compliance with financial covenants under the bank credit facility, including restrictions on the granting of liens or pledging of assets, a minimum net worth and a debt to total capitalization ratio, as well as other customary conditions and covenants. The bank credit facility restricts borrowings by subsidiaries to a maximum of \$100.0 million. The failure to satisfy any of the covenants would constitute an event of default. The bank credit facility includes other customary events of default, including without limitation, nonpayment, misrepresentation in a material respect, cross-default to other indebtedness, bankruptcy and change of control.

At June 30, 2001, the fair value of debt calculated based on a credit-adjusted spread over U.S. Treasury securities with similar maturities was \$459.7 million, compared with the balance sheet carrying amount of \$500.0 million.

7. SPECIAL CHARGES

A summary of special charges recorded in fiscal years 2000 and 1999 and changes in the related balance sheet accounts at June 30 follow (in millions):

	Balance June 30, 1998	Special Charges	Paid and Utilized	Balance June 30, 1999	Special Charges (Credit)	Paid and Utilized	Balance June 30, 2000	Paid and Utilized	Balance June 30, 2001
Workforce reductions	\$12.8	–	\$ (5.9)	\$ 6.9	\$ 15.0	\$ (6.9)	\$15.0	\$ (9.7)	\$ 5.3
Privatization costs	13.8	–	(13.8)	–	–	–	–	–	–
Suspension of development of AVLIS technology	–	\$34.7	(.5)	34.2	(1.2)	(33.0)	–	–	–
Discontinue uranium enrichment at Portsmouth plant:									
Workforce reductions	–	–	–	–	30.2	–	30.2	(5.5)	24.7
Lease turnover and other exit costs	–	–	–	–	33.5	(2.8)	30.7	(7.4)	23.3
Impairment of property, plant and equipment	–	–	–	–	62.8	(62.8)	–	–	–
	–	–	–	–	126.5	(65.6)	60.9	(12.9)	48.0
	\$26.6	\$34.7	\$(20.2)	\$41.1	\$140.3	\$(105.5)	\$75.9	\$(22.6)	\$53.3

Amounts paid and utilized include cash payments, non-cash charges for asset impairments, and liabilities incurred for incremental pension and postretirement health benefits.

Workforce Reductions

Workforce reduction plans involving 575 employees were finalized in June 2000 and resulted in special charges for severance benefits of \$15.0 million in fiscal 2000. Amounts paid and utilized with respect to the workforce reductions involving 483 employees amounted to \$9.7 million in fiscal 2001.

Discontinue Uranium Enrichment at Portsmouth Plant

In May 2001, USEC ceased uranium enrichment operations at the Portsmouth plant as an important step in the ongoing efforts to align production costs with lower market prices. USEC continues to operate the transfer and shipping facilities at the Portsmouth plant. The plan announced in June 2000 to cease uranium enrichment operations at the Portsmouth plant resulted in special charges of \$126.5 million in fiscal 2000, including asset impairments of \$62.8 million, severance benefits of \$30.2 million for workforce reductions involving 1,200 plant employees based on labor contract requirements, and lease turnover and other exit costs of \$33.5 million. In November 2000, USEC agreed to increase the amount of

severance benefits for workforce reductions at the Portsmouth plant by up to \$10.0 million by providing an additional severance benefit of \$8,400 for each employee. In fiscal 2001, amounts paid and utilized amounted to \$12.9 million, including severance benefits of \$5.5 million for workforce reductions involving 189 employees, a \$2.0 million contribution paid to the Southern Ohio Diversification Initiative for economic development in the region of the Portsmouth plant, and \$5.4 million for lease turnover activities. In fiscal 2000, amounts paid and utilized amounted to \$65.6 million, consisting principally of asset impairments applied against production equipment, leasehold improvements and other fixed assets at the Portsmouth plant.

In June 2001, DOE authorized funding for USEC to conduct winterizing, cold standby, and deposit removal contract services at the Portsmouth plant. Depending on the timing, implementation and duration of DOE's program for cold standby, costs to cease enrichment operations at the Portsmouth plant accrued by USEC in fiscal 2000 may change. Workforce reductions are delayed as a result of DOE's program to maintain the Portsmouth plant in cold standby. It is not possible to determine the effects of such program on severance and other costs associated with ceasing uranium enrichment operations.

In September 2000, USEC provided notice to terminate the electric power contract with DOE and OVEC effective April 2003 and to release power to OVEC when uranium enrichment operations at the Portsmouth plant cease. Under the terms of a supplemental letter agreement, dated March 20, 2001, OVEC released USEC from commitments to purchase electric power when enrichment operations ceased in May 2001. Upon termination of the power contract in April 2003, USEC is responsible for its pro rata share of OVEC's obligations for postretirement health benefit costs and its pro rata share of OVEC's obligations for future decommissioning and shutdown activities at the coal-burning power generating facilities owned and operated by OVEC. USEC has accrued its estimated pro rata share of such obligations. Final determinations of such costs by independent actuaries and engineering consultants could be different from the estimated amounts accrued as obligations by USEC.

Suspension of Development of AVLIS Technology

AVLIS is a uranium enrichment process which uses lasers to separate uranium isotopes. The AVLIS process was developed under a contract with DOE by the Lawrence Livermore National Laboratory ("LLNL") located in Livermore, California.

In June 1999, further development of the AVLIS enrichment technology was suspended. In connection with a comprehensive review of operating and economic factors, USEC reexamined the AVLIS technology, performance, prospects, risks and growing financial requirements as well as the economic impact of competitive marketplace dynamics and concluded that the returns were not sufficient to outweigh the risks and ongoing capital expenditures necessary to develop and construct an AVLIS plant.

USEC terminated AVLIS efforts with its contractors, implemented workforce reductions and conducted an orderly ramp-down of AVLIS activities at LLNL in California. The suspension of AVLIS resulted in a special charge of \$34.7 million in fiscal 1999 for contract terminations, shutdown activities and employee severance and benefit arrangements, of which \$33.5 million had been paid as of June 30, 2000. A cost savings of \$1.2 million was restored to income in fiscal 2000.

8. ENVIRONMENTAL MATTERS

Environmental compliance costs include the handling, treatment and disposal of hazardous substances and wastes. Pursuant to the USEC Privatization Act, environmental liabilities associated with plant operations prior to July 28, 1998, are the responsibility of the U.S. Government, except for liabilities relating to certain identified wastes generated by USEC and stored at the plants. DOE remains responsible for decontamination and decommissioning of the plants.

Depleted Uranium

USEC accrues estimated costs for the future disposition of depleted uranium based on estimates for transportation, conversion and disposal. Pursuant to the USEC Privatization Act, depleted uranium generated by USEC through July 28, 1998, was transferred to DOE. USEC stores depleted uranium generated since July 28, 1998, at the plants and continues to evaluate various proposals for its disposition. The accrued liability included in other long-term liabilities amounted to \$66.2 million at June 30, 2001, and \$48.6 million at June 30, 2000.

In June 1998, USEC paid \$50.0 million to DOE, and DOE assumed responsibility for disposal of a certain amount of depleted uranium generated by USEC from October 1998 to September 2005. The payment resulted in deferred costs for depleted uranium that are being amortized as charges against production costs using a straight line method over the term of the agreement. The remaining balance amounted to \$27.1 million at June 30, 2001, and \$35.4 million at June 30, 2000.

Other Environmental Matters

USEC's operations generate hazardous, low-level radioactive and mixed wastes. The storage, treatment and disposal of wastes are regulated by federal and state laws. USEC utilizes offsite treatment and disposal facilities and stores wastes at the plants pursuant to permits, orders and agreements with DOE and various state agencies. The accrued liability for the treatment and disposal of stored wastes generated by USEC's operations and included in other liabilities amounted to \$4.7 million at June 30, 2001 and at June 30, 2000.

Nuclear Indemnification

DOE is required to indemnify USEC against claims for public liability (i) arising out of or in connection with activities under the lease, including domestic transportation and (ii) arising out of or resulting from a nuclear incident or precautionary evacuation. DOE's obligations are capped at the \$9.4 billion statutory limit set forth in the Price-Anderson Act for each nuclear incident or precautionary evacuation occurring inside the United States. The Price-Anderson Act is scheduled to expire August 2002. USEC expects indemnification legislation will be reauthorized.

Contract Services for DOE

USEC provides contract services for DOE at the plants as a contractor and as a subcontractor. Contract services include environmental restoration, waste management and, beginning in fiscal 2001, winterization, cold standby and deposit removal at the Portsmouth plant. Payments by DOE and DOE contractors to USEC for contract services are based on actual costs incurred and amounted to \$35.3 million, \$34.2 million, and \$38.3 million in fiscal years 2001, 2000, and 1999, respectively.

9. COMMITMENTS AND CONTINGENCIES

Power Contracts and Commitments

In September 2000, USEC began purchasing a substantial portion of the electric power for the Paducah plant at fixed rates pursuant to a power purchase agreement with TVA. TVA provides electric power at fixed contract prices with capacity varying monthly from 300 to 1,780 megawatts. Prices are fixed from September 2000 until May 2006. In order to reduce power costs, USEC substantially reduces production and the related power load at the Paducah plant in the summer months when the cost of power is high. Subject to prior notice, TVA may interrupt power to the Paducah plant, except no interruption is allowed in the summer months. Under the agreement, amounts paid to TVA for power purchased in fiscal 2001 were reduced by a deferred payment obligation. At June 30, 2001, the deferred payment obligation amounted to \$40.8 million, of which \$19.6 million was included in current liabilities as part of deferred revenue and advances from customers. USEC has secured the obligation, as long as it is outstanding, by transferring

title to uranium inventories with an equivalent value to TVA. The obligation and related interest is scheduled to be satisfied in connection with the sale of the SWU component of LEU to TVA under a requirements contract in fiscal years 2002 through 2004.

In fiscal 2001, USEC purchased electric power for the Portsmouth plant from OVEC, and purchased a portion of the electric power for the Paducah plant from EEI. DOE transferred the benefits of the OVEC and EEI power purchase contracts to USEC. Cost for electric power purchased from OVEC and EEI are based on actual costs incurred by OVEC and EEI.

USEC is obligated, whether or not it takes delivery of power, to make minimum annual payments for the purchase of power estimated as follows (in millions):

Fiscal Years Ending June 30,	
2002	\$ 254.9
2003	273.4
2004	251.7
2005	258.9
2006	234.6
	<u>\$1,273.5</u>

Legal Matters

On October 27, 2000, a federal securities lawsuit was filed against USEC in the U.S. District Court for the Western District of Kentucky, Paducah Division. In June 2001, the lawsuit was transferred to the U.S. District Court for the Southern District of Maryland. The lawsuit names as defendants USEC and certain of its officers and seven underwriters involved in the initial public offering of common stock. Additional lawsuits of a similar nature have been filed in the same court. The plaintiffs in each lawsuit seek to represent a class of purchasers of USEC's common stock between July 23, 1998, and December 2, 1999. On July 23, 1998, USEC's common stock began trading in connection with the initial public offering. The lawsuits generally allege that certain statements in the registration statement and prospectus for the initial public offering were materially false and misleading because they misrepresented and failed to

disclose certain adverse material facts, risks and uncertainties. The plaintiffs seek compensatory damages. USEC believes that the allegations are without merit and intends to defend itself vigorously, and that the outcome of these lawsuits will not have a material adverse effect on its financial position or results of operations.

In June 2001, USEC received notices from the Ohio State Department of Taxation asserting deficiencies in personal property tax payments for calendar years 2000 and 1999. The total additional property taxes asserted amount to \$13.3 million plus interest and relate principally to certain inventories USEC believes are exempt from personal property taxes in Ohio. USEC believes it has meritorious defenses to the asserted deficiencies and plans to file petitions for reassessment challenging the additional property taxes.

USEC is subject to various other legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. While the outcome of these claims cannot be predicted with certainty, USEC does not believe that the outcome of any of these legal matters will have a material adverse effect on its financial position or results of operations.

Lease Commitments

Total costs incurred under the lease with DOE for the plants and leases for office space and equipment aggregated \$7.2 million, \$7.1 million and \$8.1 million in fiscal years 2001, 2000 and 1999, respectively. Minimum lease payments are estimated at \$5 million for each of the next five fiscal years.

USEC has the right to extend the lease for the plants indefinitely at its sole option and may terminate the lease in its entirety or with respect to one of the plants at any time upon two years' notice. Upon termination of the lease, USEC is responsible for certain lease turnover activities, including documentation of the condition of the plants and termination of facility operations. Lease turnover costs are accrued and charged to production costs over the expected lease period which for the Paducah plant is estimated to extend through calendar year 2008. Lease turnover costs for the Portsmouth plant were accrued over the productive life of the plant and as part of a special charge in fiscal 2000. Accrued costs included in other liabilities amounted to \$35.7 million at June 30, 2001 and \$32.5 million at June 30, 2000.

Employee Matters

Two labor unions represent 51% of the employees at the plants. The collective bargaining agreement covering 660 hourly employees at the Paducah plant represented by the Paper, Allied-Industrial, Chemical and Energy Workers International Union is scheduled to expire July 31, 2001. The contract renewal process is underway.

10. PENSION AND POSTRETIREMENT HEALTH AND LIFE BENEFITS

In fiscal 1999, the operations and maintenance contract with Lockheed Martin Utility System ("LMUS"), a subsidiary of Lockheed Martin Corporation, was terminated by USEC. Most employees of LMUS became employees of USEC. Pension and postretirement health and life benefit obligations and related plan assets were transferred from plans sponsored by Lockheed Martin Corporation to plans sponsored by USEC. The aggregate of the fair values of plan assets transferred was equivalent to the combined pension and postretirement health and life benefit obligations transferred to USEC based on discount rates established by the Pension Benefit Guaranty Corporation and other actuarial assumptions. Plan assets for pension and postretirement health and life benefit plans are maintained in trusts and consist mainly of common stock and fixed-income investments.

There are 7,600 employees and retirees covered by defined benefit pension plans providing retirement benefits based on compensation and years of service, and 3,400 employees, retirees and dependents covered by postretirement health and life benefit plans. DOE retained the obligation for postretirement health and life benefits for workers who retired prior to July 28, 1998.

Changes in benefit obligations and plan assets in fiscal years 2001 and 2000 and the funded status of the plans at June 30 follow (in millions):

	Fiscal Years Ended June 30,			
	Defined Benefit Pension Plans		Postretirement Health and Life Benefit Plans	
	2001	2000	2001	2000
Changes in Benefit Obligations				
Obligations at beginning of fiscal year	\$414.2	\$ 430.0	\$ 128.9	\$ 130.0
Actuarial (gain) loss	22.6	(33.4)	7.2	6.6
Change in attribution period	—	—	—	(22.6)
Service cost	9.4	11.5	7.1	6.9
Interest cost	33.7	32.3	12.4	10.2
Benefits paid	(27.4)	(26.2)	(2.0)	(2.2)
Obligations at end of fiscal year	452.5	414.2	153.6	128.9
Changes in Plan Assets				
Fair value of plan assets at beginning of fiscal year	624.0	511.0	38.0	37.0
Actual return on plan assets	(22.3)	101.3	4.5	1.0
USEC contributions	.1	.4	1.5	2.2
Fair value of plan assets transferred	—	37.5	—	—
Benefits paid	(27.4)	(26.2)	(2.0)	(2.2)
Fair value of plan assets at end of year	574.4	624.0	42.0	38.0
Funded (unfunded) status	121.9	209.8	(111.6)	(90.9)
Unrecognized prior service costs (benefit)	.8	—	(9.4)	(20.5)
Unrecognized net actuarial (gains) losses	(45.8)	(151.6)	(3.7)	4.9
Prepaid (accrued) benefit costs at June 30	\$ 76.9	\$ 58.2	\$(124.7)	\$(106.5)

The expected cost of providing pension benefits is accrued over the years employees render service, and actuarial gains and losses are amortized over the employees' average future service life.

In fiscal 2000, the attribution period for postretirement health and life benefit obligations was changed from 10 years of service to 10 years of service commencing at age 40 or from date of hire if after age 40. There were no changes in

the postretirement health or life benefits. The change in the attribution period reduced the benefit obligation by \$22.6 million in fiscal 2000 and reduced net benefit plan costs by \$2.4 million in fiscal 2001 and \$2.1 million in fiscal 2000. Actuarial gains and losses and prior service costs or benefits are amortized over the average remaining years of service until the date of full benefit eligibility.

The components of net benefit costs (income) and the assumptions used in the calculations of benefit obligations at June 30 follow (dollars in millions):

	Fiscal Years Ended June 30,			
	Defined Benefit Pension Plans		Postretirement Health and Life Benefit Plans	
	2001	2000	2001	2000
Service cost	\$ 9.4	\$11.5	\$ 7.1	\$ 6.9
Interest cost	33.7	32.3	12.4	10.2
Expected return on plan assets	(55.0)	(48.6)	(3.4)	(3.2)
Amortization of actuarial (gains) losses	(7.3)	—	—	—
Amortization of prior service costs (credit)	—	—	(2.4)	(2.1)
Net benefit costs (income)	\$ (19.2)	\$ (4.8)	\$ 13.7	\$ 11.8
Discount rate	7.5%	8.0%	7.5%	8.0%
Expected return on plan assets	9.0	9.0	9.0	9.0
Compensation increases	4.5	4.5	4.5	4.5

The healthcare cost trend rate used to measure the post-retirement health benefit obligation is 7% in fiscal 2002 and is assumed to decline gradually to 5% over the next five years and then remain level. A one-percentage-point change in the assumed healthcare cost trend would change annual costs by \$3.2 million and change the benefit obligation by \$26.6 million.

USEC sponsors 401(k) and other defined contribution plans for employees. Employee contributions are matched at established rates. Amounts contributed are invested in securities and administered by independent trustees. USEC's matching contributions amounted to \$5.6 million, \$5.9 million, and \$5.6 million in fiscal years 2001, 2000, and 1999, respectively.

USEC provides executive officers, through nonqualified plans, additional pension benefits in excess of qualified plan limits imposed by tax law. The excess pension benefits are unfunded. The actuarial present value of projected benefit obligations for excess pension benefits amounted to \$6.7 million at June 30, 2001, and \$2.6 million at June 30, 2000. Under a 401(k) restoration plan, executive officers contribute and USEC matches contributions in excess of amounts eligible under the 401(k) plan. Costs for plans providing excess pension benefits, 401(k) restoration and other supplemental benefits for executive officers amounted to \$1.3 million in fiscal 2001 and \$1.1 million in fiscal 2000.

11. STOCKHOLDERS' EQUITY

Common Stock

Changes in the number of shares of common stock outstanding follow (in thousands):

	Shares Issued	Treasury Stock	Shares Outstanding
Balance June 30, 1998	—	—	—
Initial public offering	100,000	—	100,000
Repurchase of common stock	—	(1,142)	(1,142)
Common stock issued	318	—	318
Balance at June 30, 1999	100,318	(1,142)	99,176
Repurchase of common stock	—	(16,972)	(16,972)
Common stock issued	2	272	274
Balance at June 30, 2000	100,320	(17,842)	82,478
Repurchase of common stock	—	(2,819)	(2,819)
Common stock issued	—	907	907
Balance at June 30, 2001	100,320	(19,754)	80,566

Preferred Stock Purchase Rights

In April 2001, the Board of Directors approved a shareholder rights plan, under which shareholders of record May 9, 2001, received rights that initially trade together with USEC common stock and are not exercisable. In the absence of further action by the Board, the rights generally would become exercisable and allow the holder to acquire USEC common stock at a discounted price if a person or group acquires 15% or more of the outstanding shares of USEC common stock or commences a tender or exchange offer to acquire 15% or more of the common stock of USEC. However, any rights held by the acquirer would not be exercisable.

The Board of Directors may direct USEC to redeem the rights at \$.01 per right at any time before the tenth day following the acquisition of 15% or more of USEC common stock.

Compensation Plans

In February 1999, stockholders approved the USEC Inc. 1999 Equity Incentive Plan, under which 9 million shares of common stock were reserved for issuance over a 10-year period, including incentive stock options, nonqualified stock options, restricted stock or stock units, performance awards and other stock-based awards.

Grants of restricted stock, net of forfeitures, amounted to 273,000 shares, 110,000 shares and 318,000 shares and resulted in deferred compensation, based on the fair market value of common stock at the date of grant, of \$.3 million, \$1.7 million and \$4.4 million in fiscal years 2001, 2000, and 1999, respectively. Sale of such shares is restricted prior to the date of vesting. Deferred compensation is amortized to expense on a straight-line basis over the vesting period.

A summary of stock options outstanding in fiscal years 2001 and 2000 follows (shares in thousands):

	Number of Shares	Weighted-Average Exercise Price
Balance at June 30, 1999	1	\$13.74
Options granted	4,555	8.47
Options forfeited	(377)	10.81
Balance June 30, 2000	4,179	8.27
Options granted	108	4.33
Options exercised	(67)	4.69
Options forfeited	(972)	9.69
Balance June 30, 2001	3,248	\$ 7.78

Options outstanding and options exercisable at June 30, 2001, follow (shares in thousands):

Exercise Price	Options Outstanding	Remaining Life in Years	Options Exercisable
\$ 4.69	1,724	8.8	530
\$ 11.88	1,401	8.0	291
\$4 – \$14	123	8.3	15
	3,248	8.4	836

In February 1999, stockholders approved the USEC Inc. 1999 Employee Stock Purchase Plan under which 2.5 million shares of common stock can be purchased over a 10-year period by participating employees at 85% of the lower of the market price at the beginning or the end of each six-month offer period. Employees can elect to designate up to 10% of their compensation to purchase common stock under the plan. There were 514,000 shares purchased by participating employees in fiscal year 2001 and 140,000 shares purchased in fiscal 2000.

Compensation expense for employee stock compensation plans is measured using the intrinsic value-based method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued for Employees." Under the disclosure provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("FAS 123"), pro forma net income assuming compensation expense was recognized under FAS 123 would have been \$1.4 million (or \$.02 per share) lower than reported in fiscal 2001 and \$.9 million (or \$.01 per share) lower than reported in fiscal 2000. Under FAS 123, compensation expense is based on the fair value of stock options at the date of grant using the Black-Scholes option pricing model and is amortized to expense over the vesting period. The fair value of stock options granted was \$.1 million in fiscal 2001 and \$6.4 million in fiscal 2000. Assumptions used for options outstanding in fiscal years 2001 and 2000 follow:

	Fiscal Years Ended June 30,	
	2001	2000
Risk-free interest rate	5.5%	6.5%
Expected dividend yield	7-10%	9-12%
Expected volatility	50-60%	37-59%
Expected option life	6 years	6 years

Privatization

An exit dividend of \$1,709.4 million was paid to the U.S. Government at the time of the initial public offering in July 1998. The amount of the exit dividend in excess of retained earnings was recorded as a reduction of excess of capital over par value.

Pursuant to the USEC Privatization Act, depleted uranium generated by USEC at the time of the initial public offering in July 1998 was transferred to DOE, and, in fiscal 1999, the accrued liability of \$373.8 million for the disposition of depleted uranium was transferred to stockholders' equity.

12. QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table summarizes quarterly and annual results of operations (in millions, except per share data):

	Sept. 30	Dec. 31	March 31	June 30	Fiscal Year
Fiscal Year Ended June 30, 2001					
Revenue	\$226.8	\$387.1	\$243.1	\$286.9	\$ 1,143.9
Cost of sales	197.0	335.2	211.5	248.0	991.7
Gross profit	29.8	51.9	31.6	38.9	152.2
Advanced technology development costs	3.1	2.0	2.9	3.4	11.4
Selling, general and administrative	13.0	11.1	11.2	13.5	48.8
Operating income	13.7	38.8	17.5	22.0	92.0
Interest expense	8.6	8.8	8.6	9.2	35.2
Other (income) expense, net	(2.1)	(2.6)	(2.2)	(1.2)	(8.1)
Provision (credit) for income taxes	2.6	11.7	(34.3) ⁽¹⁾	6.5	(13.5)⁽¹⁾
Net income	\$ 4.6	\$ 20.9	\$ 45.4	\$ 7.5	\$ 78.4
Net income per share – basic and diluted	\$.06	\$.26	\$.56	\$.09	\$.97
Average number of shares outstanding	81.3	80.6	80.4	80.5	80.7
Fiscal Year Ended June 30, 2000					
Revenue	\$230.9	\$447.6	\$281.8	\$529.1	\$1,489.4
Cost of sales	186.4	377.4	226.0	446.5	1,236.3
Uranium inventory valuation adjustment	–	–	–	19.5	19.5
Gross profit	44.5	70.2	55.8	63.1	233.6
Special charges	–	–	–	140.3 ⁽²⁾	140.3 ⁽²⁾
Advanced technology development costs	1.4	2.6	2.7	4.7	11.4
Selling, general and administrative	12.2	11.2	11.7	13.8	48.9
Operating income (loss)	30.9	56.4	41.4	(95.7)	33.0
Interest expense	8.5	9.8	10.9	8.9	38.1
Other (income) expense, net	(2.8)	(2.9)	(2.6)	(2.2)	(10.5)
Provision (credit) for income taxes	9.1	16.9	10.5	(40.0)	(3.5)
Net income (loss)	\$ 16.1	\$ 32.6	\$ 22.6	\$ (62.4)	\$ 8.9
Net income (loss) per share – basic and diluted	\$.16	\$.36	\$.25	\$ (.74)	\$.10 ⁽³⁾
Average number of shares outstanding	97.7	90.6	89.6	84.7	90.7

1) The provision for income taxes in fiscal 2001 includes a special income tax credit of \$37.3 million (or \$.46 per share) resulting from changes in the estimated amount of deferred income tax benefits that arose from the transition to taxable status.

2) The plan to cease uranium enrichment operations at the Portsmouth plant resulted in special charges of \$126.5 million (\$79.3 million or \$.87 per share after tax) in fiscal 2000, including asset impairments of \$62.8 million, severance benefits of \$30.2 million and lease turnover and other exit costs of \$33.5 million.

Workforce reduction plans involving 575 employees resulted in special charges for severance benefits of \$15.0 million (\$9.4 million or \$.10 per share after tax) in fiscal 2000.

3) Net income per share in fiscal 2000 does not equal the sum of the quarters because of changes in the number of shares outstanding from the repurchase of common stock.

To USEC Inc.:

We have audited the accompanying consolidated balance sheets of USEC Inc. (a Delaware Corporation) as of June 30, 2001 and 2000, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three fiscal years in the period ended June 30, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of USEC Inc. as of June 30, 2001 and 2000, and the results of its operations and its cash flows for each of the three fiscal years in the period ended June 30, 2001, in conformity with accounting principles generally accepted in the United States.

Arthur Andersen LLP

Vienna, Virginia

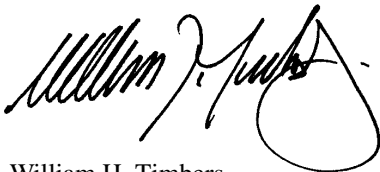
July 26, 2001

The financial statements of USEC Inc. were prepared by management, which is responsible for their integrity and objectivity. The statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances and necessarily include some amounts that are based on the best estimates and judgments of management.

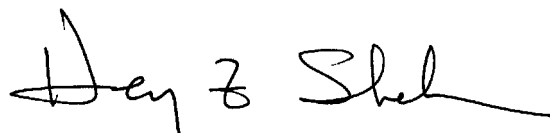
The system of internal controls is designed to provide reasonable assurance as to the reliability of financial records and the protection of assets. This system is augmented by written policies and guidelines, an internal audit program and the careful selection and training of qualified personnel. It should be recognized, however, that there are inherent limitations in the effectiveness of any internal control system. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to the preparation of reliable financial statements and safeguarding of assets. Further, because of changing conditions, internal control system effectiveness may vary over time.

Arthur Andersen LLP was engaged to audit the consolidated financial statements of USEC Inc. and issue reports thereon. Their audits included developing an overall understanding of the accounting systems, procedures and internal controls and conducting tests and other auditing procedures sufficient to support their report on the consolidated financial statements.

The adequacy of financial controls and the accounting principles employed in financial reporting are under the general oversight of the Audit, Finance and Corporate Responsibility Committee of the Board of Directors. No member of the committee is an officer or employee of USEC Inc. The independent public accountants and the internal auditors have direct access to the Audit, Finance and Corporate Responsibility Committee, and they meet with the committee from time to time, with and without management present, to discuss accounting, auditing and financial reporting matters.



William H. Timbers
President and Chief Executive Officer



Henry Z. Shelton, Jr.
Senior Vice President and Chief Financial Officer

July 26, 2001

Shareholder Information

Stock Exchange Listing

USEC Inc. common stock is listed and traded on the New York Stock Exchange under the ticker symbol USU. Options are listed and traded on the Chicago Board of Exchange, the American Stock Exchange and the Pacific Stock Exchange. As of August 15, 2001, the Company had approximately 29,000 beneficial holders of its common stock.

Annual Meeting

The Annual Meeting of Shareholders will be held at 10 a.m. November 7, 2001 at the Naval Heritage Center in Washington, D.C. The Center is located on the first floor of 701 Pennsylvania Avenue, N.W., and is convenient to the Archives/Navy Memorial Metro stop.

Annual Report on Form 10-K

Upon written request, USEC Inc. will provide without charge a copy of its Annual Report on Form 10-K, as filed with the Securities and Exchange Commission. Requests should be sent to the attention of Investor Relations at the address listed below. The Form 10-K is also available on the Company's Internet site at www.usec.com

Corporate Headquarters and Mailing Address

USEC Inc.

Two Democracy Center

6903 Rockledge Drive
Bethesda, MD 20817-1818
Phone: (301) 564-3200
Fax: (301) 564-3211

Internet Home Page

The Company maintains an Internet site at www.usec.com that contains a substantial amount of information about USEC and its activities, news releases, and financial information. There are also links to our filings with the Securities and Exchange Commission. E-mail inquiries to USEC Inc. may be addressed to: corpcomm@usec.com

Investor Relations

Information requests from security analysts and other members of the professional financial community may be directed to: Investor Relations (301) 564-3238. E-mail inquiries should be addressed to: financial@usec.com

Stock Held in Brokerage Account or "Street Name"

When you purchase stock and it is held for you by your broker, it is listed with the Company in the broker's name, or "street name." Most USEC Inc. common shares are held in street name accounts. USEC does not know the identity of individual shareholders who hold shares in this manner; we simply know that a broker holds a certain number of shares that may be for any number of individuals. If you hold your stock in street name, you receive all dividend payments, annual reports and proxy materials through your broker. Therefore, if your shares are held in this manner, any questions you may have about your shares should be directed to your broker.

Transfer Agent & Registrar

USEC Inc. shareholder records are maintained by our transfer agent, EquiServe. Shareholders of record with inquiries relating to stock records, stock transfer,

changes of ownership, changes of address, dividend payments and consolidation of accounts should contact:

EquiServe

Shareholder Services

Mail Stop: 45-02-64
P.O. Box 43010
Providence, RI 02940-3010
Toll-free telephone: (888) 485-2938
Internet: www.equiserve.com

Dividends

Dividends on USEC Inc. common stock are paid as declared by the Board of Directors. Dividends are typically paid on the 15th of the month in March, June, September and December.

Direct Stock Purchase and Dividend Reinvestment Plan

USEC is pleased to offer the USEC-Invest Plan that enables new and existing shareholders to build ownership in the Company over time. This direct stock purchase and dividend reinvestment plan is designed for individual investors who wish to minimize their transaction costs when buying USEC stock. If you do not currently own registered shares in USEC, you may use USEC-Invest to buy your first shares directly from the Company. The minimum initial investment is \$250. For more information and a prospectus, call (888) 485-2938 or go on-line to www.usec.com and click on the Investor Relations section.

Independent Auditors

Arthur Andersen LLP

Vienna, VA



James R. Mellor,
Chairman of the Board, USEC
Inc. Retired Chairman and
Chief Executive Officer,
General Dynamics Corporation



William H. Timbers
President and Chief
Executive Officer, USEC Inc.



Joyce F. Brown
President, Fashion Institute
of Technology of the State
University of New York



John R. Hall
Retired Chairman and
Chief Executive Officer,
Ashland, Inc.



Dan T. Moore, III
President, Dan T. Moore
Company, Inc.



W. Henson Moore
President and Chief Executive
Officer, American Forest and
Paper Association



William H. White
President and Chief
Executive Officer,
Wedge Group Inc.



James D. Woods
Chairman Emeritus
Baker Hughes, Inc.

Executive Officers

William H. Timbers
President and
Chief Executive Officer

Dennis R. Spurgeon
Executive Vice President and
Chief Operating Officer

Robert J. Moore
Senior Vice President and
General Counsel

Philip G. Sewell
Senior Vice President

Henry Z. Shelton, Jr.
Senior Vice President and
Chief Financial Officer

James N. Adkins, Jr.
Vice President,
Services and Projects

Dennis J. Blair
Vice President,
Human Resources
and Administration

J. Morris Brown
Vice President,
Operations

Gary G. Ellsworth
Vice President,
Government Relations

Timothy B. Hansen
Vice President,
Deputy General
Counsel and Secretary

Robert Van Namen
Vice President,
Marketing and Sales

Michael T. Woo
Vice President,
Strategic Development

Charles B. Yulish
Vice President,
Corporate Communications

Board Committees

(*indicates the chair of each committee)

Audit, Finance and Corporate Responsibility

James D. Woods*
Joyce F. Brown
John R. Hall

Compensation

John R. Hall*
Joyce F. Brown
James D. Woods

Nominating and Governance

James R. Mellor*
John R. Hall
W. Henson Moore

Regulatory Affairs

W. Henson Moore*
Dan T. Moore
William H. White

Technology

Dan T. Moore*
James R. Mellor
William H. White

William H. White has decided not to stand for reelection to the Board of Directors at the Annual Meeting of Shareholders, and will leave the Board at that time. The Board would like to express its sincere appreciation for Bill's service and valued counsel during his three-year tenure.



USEC Inc.

Two Democracy Center
6903 Rockledge Drive
Bethesda, Maryland
20817-1818

www.usec.com